

# Economic Law as an Economic Good

Its Rule Function and its Tool Function in the Competition of Systems

Bearbeitet von  
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1. Auflage 2009. Taschenbuch. ca. 450 S. Paperback  
ISBN 978 3 86653 116 1  
Format (B x L): 16 x 24 cm  
Gewicht: 688 g

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Wirtschaftsrecht](#)

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sellier.  
european law  
publishers

Der Druck dieses Werkes wurde durch die Fritz Thyssen Stiftung gefördert.

ISBN (print) 978-3-86653-116-1

ISBN (eBook) 978-3-86653-858-0

The Deutsche Nationalbibliothek lists this publication in the Deutsche Nationalbibliografie; detailed bibliographic data are available on the Internet at <http://dnb.d-nb.de>.

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Design: Sandra Sellier, Munich. Production: Karina Hack, Munich. Typeface: Goudy Old Style and Goudy Sans from Linotype. Printing and binding: Friedrich Pustet KG, Regensburg. Printed on acid-free, non-ageing paper. Printed in Germany.

## Introduction



# Economic Law as an Economic Good: Its Rule Function and its Tool Function in the Competition of Systems

Karl M. Meessen\*

To some extent, business can choose the economic law it wishes to govern its activities. The traditional way of doing so is to directly choose the contract law applicable to a specific transaction, subject, of course, to such internationally mandatory rules of law as may be applicable under the *lex fori* or the *lex arbitri*.<sup>1</sup> Choosing contract law in that way has its implications for the legal services industry. Hence those responsible for the making of contract law in England and in the state of New York, to name but the two legal systems often chosen in international transactions, make sure that the respective laws do not lose their attractiveness by an overdose of well intended or just ideosyncratic restrictions on the freedom of contract. There is, however, a second more indirect way of choosing the applicable law. Technically speaking, it is by choosing the “points of contract” liable to trigger the applicability of one or more particular economic laws through localizing business activities in one or more particular states. That can mean avoiding investment of capital in places where there is a political risk of expropriation, or it can mean avoiding trading in goods at places where obtaining government consent to certain activities, or the enforcement of contracts, is dependent on the payment of bribes. Put the other way around, business is usually attracted to places where a competitive environment welcomes new entrants into the market, and thus, where effectiveness, innovativeness and other virtues of business performance are likely to be rewarded.

Governments, or the clever ones among them, are aware of the factors guiding business activities. In the course of adopting and enforcing economic legislation, they seek to attract business activities in order to increase the national income (and fiscal revenues), generate employment opportunities and, very generally, please voters.<sup>2</sup> Hence, economic law may, as suggested in the title of this book, be considered an economic good. It is a public good offered in the expectation of secondary benefits to be derived from the localization of business activities throughout the world.

The subtitle states the two functions of economic law. Economic law is not only a “tool”, that is, an instrument in the pursuit of such interjurisdictional competition among states and supranational organizations, such as the European Union. Economic law also

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<sup>1</sup> Meessen, *Economic Law in Globalizing Markets* (2004), p. 145, 295; (generally) p. 139 et seq., 293 seq.

<sup>2</sup> Meessen (note 1), p. 9 et seq. with further references.

has a rule function in the competition of systems. The way that function operates varies depending on the context.

Most of the rules of WTO law, for instance, promote not only the competition among enterprises but also interjurisdictional competition as part of a broader competition of systems. The more freely business can choose the location of its activities, the more pressure it exerts upon states to enhance the attractiveness of the economic laws they are making. That pressure results from the increased ease with which business can relocate its activities. In fact, such easing of exit from, and entry into, markets is the essential contribution WTO law is making to the competition of systems. International standards, whether set by a WTO agreement or any other convention, are ambivalent. They ease cross-border trade but, at the same time, they bring to an end the competition for the right standard. That competition for standards can evolve as a race to the top or as a race to the bottom. The metaphorical distinction between top and bottom is misleading in so far as it is an open question whether business values more highly the top of tight regulation or the bottom of loose regulation. It is for the market, in a Hayekian process of discovery,<sup>3</sup> to find out the direction the race will take.

The banking crisis of 2008 is at present developing into a fully-fledged economic crisis of worldwide dimension. In tackling the current crisis, there is much talk of coordinated action. The action so far undertaken on state level, however, clearly bears witness to another lively round in the ongoing competition of systems. Given an increased role of governments within the economy, competition among them is, if anything, bound to gain further momentum.

Whenever the making of economic law is involved, heed should be taken of its dual function as a rule and as a tool in the competition of systems. Assessing those secondary functions of each and every rule of economic law may also contribute to the proper application of the respective rule in legal practice. In addition, economic and political theory may draw benefit from a better understanding of the political economy of the competitive, as opposed to the harmonized or cartelized, making of economic law.

The very elusiveness of the various functions of economic law as a rule and as a tool is at the core of this collection of essays. The essays assembled in this book were, with two exceptions, elaborated on the basis of papers presented and extensively discussed at a symposium of academics and practitioners of law and economics, from inside and outside Germany, held in Düsseldorf from 2 to 4 November 2007. Before giving a survey of those studies (Section B), it may be appropriate to take, in Section A, a look at the notion of competition since competition is the element common to both the interaction among companies in the market and the interaction among states and supranational organizations. The survey of the papers to be given in Section B will be followed by some tentative conclusions sketched out at the end of this introductory note (Section C).

## A. The Competition Principle

To lawyers familiar with competition law, and to economists familiar with competition theory, the term “competition” refers to the competition between enterprises in the framework of such national or supranational competition law or laws as may be applicable

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<sup>3</sup> Hayek, *Der Wettbewerb als Entdeckungsverfahren* (1968).

to the particular case situation. The competition between enterprises certainly is the type of competition most extensively discussed and most sophisticatedly analysed in scientific theory. But it is just one type of competition among many others.

The process of competition is in fact a general phenomenon characterizing a type of interaction among human beings or rather among organisms of any kind. Animals compete for food, for sexual partners and for a place to rest. Even plants stretch themselves to reach more sunshine than neighbouring plants. Bacteria and other micro-organisms fight for supremacy. The evolution of organic nature has aptly been described as a quest for the “survival of the fittest” ever since *Charles Darwin* incorporated that term in the 4<sup>th</sup> edition of 1869 of his “*The Origin of Species*” of 1859. The underlying theory has remained uncontested. It has been refined and confirmed by modern molecular biology.<sup>4</sup>

Competition is a principle of life. In that general perception, competition can be described as an open-ended process involving two or more players of an equal or a different structure, all of them striving for some benefit, even if at the expense of other players. The competitive process tends to fully exploit physical and intellectual resources of each player. The resulting high performance continuously generates positive externalities in terms of biological, scientific, technical and economic progress to the benefit of a multitude of human beings and/or other organisms.

If asked to give an example of competition, competition in sports and competition in politics probably first spring to the mind of anyone who does not happen to be an economist or a lawyer. Sports may even have an archetypical value in explaining what competition is about. The time element in sports is most telling, and so is its rule bound, though not always rule abiding, character. In politics, rule abidance is less common. Nonetheless, it may produce comparable rewards in terms of power and perks.

As to the competition of systems, a struggle among states and other political units for superiority can be observed throughout the known history of mankind. Internecine wars have been, and still are, its common feature. At times of peace, a considerable amount of struggle is going on as well, just at a level short of warfare.<sup>5</sup> There is nothing new about that competition to proceed by way of forging one’s own legal, social, cultural, economic and/or political system. As a result of worldwide liberalization, it has, however, become more intense during the last couple of decades.

In economic literature, a decisive insight is owed to one of those short seminal articles that have from time to time offered a new paradigm to the economic understanding of political and social processes. The reference is to *Charles M. Tiebout’s* 9-page piece of 1956,<sup>6</sup> in which he explained some of the factors liable to channel economic activity to certain locations. While Tiebout discussed a phenomenon observed on the level of local government, the more voluminous studies that followed his pioneering article examined the competition among states within a federation,<sup>7</sup> among member states of

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<sup>4</sup> For a recent assessment see Kirschner & Gerhart, *The Plausibility of Life* (2005); see also Edelman, *Neural Darwinism* (1987); for the common elements of economic and biological phenomena see Hayek, *The Sensory Order* (1952).

<sup>5</sup> Morgenthau & Thompson, *Politics among Nations*, 6<sup>th</sup> ed. (1985); for recent studies with an emphasis on economic aspects see Porter, *The Competitive Advantage of Nations* (1990); Olson, *Power and Prosperity* (2000).

<sup>6</sup> Tiebout, *A Pure Theory of Local Expenditures*, 64 *J.Pol.Econ.* 416 (1956).

<sup>7</sup> Bratton & McCahery, *The New Economics of Jurisdictional Competition, Devolutionary Federalism in a Second-Best World*, 86 *Geo.L.J.* 201 (1997).