Alternative Grounds: Epstein's Discrimination Analysis in Other Market Settings

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INTRODUCTION

In *Forbidden Grounds*,[1] Richard Epstein argues that we should repeal laws prohibiting various forms of discrimination in contemporary labor markets. However, the theories underlying Epstein's argument could have much broader ramifications. As John Donohue observes in his excellent review: "Because Epstein argues from libertarian first principles, . . . he could have written the same book, *mutatis mutandis*, advocating the repeal of the laws prohibiting drug use, sodomy, pornography, prostitution, gambling, or dueling."[2] In particular, he also might have argued for the repeal of antidiscrimination laws in other markets. In this Article, I would like to focus my energy on how Epstein's discrimination analysis plays out in four other market contexts: (1) historical labor markets (circa

* Professor, Stanford Law School. John Donohue, Lawrence Friedman, Pam Karlin, Richard Sander, Peter Siegelman, and Eric Talley provided helpful comments.

1. RICHARD A. EPSTEIN, FORBIDDEN GROUNDS: THE CASE AGAINST EMPLOYMENT DISCRIMINATION LAWS (1992).

2. John J. Donohue III, *Advocacy Versus Analysis in Assessing Employment Discrimination Law*, 44 STAN. L. REV. 1583, 1586 (1992).

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1964); (2) public accommodations; (3) housing; and (4) new car markets. Applying Epstein's theory to these different market settings exposes limitations of Epstein's analysis.

I. A History of Mandated Discrimination

One of the book's great analytic strengths is that Epstein provides an internally consistent historical explanation for why freedom of contract did not eradicate the invidious effects of race discrimination prior to the advent of civil rights laws. Although Gary Becker and other theorists have suggested that competition should drive discriminators from the market,[3] none has provided an explanation for the long historical persistence of discrimination prior to the passage of Title VII in 1964. Thus, in characterizing the conclusions of a perfect competition model fashioned after Gary Becker's "Economics of Discrimination," Kenneth Arrow argues:

> As a result, the competitive effect just studied assumes an exaggerated form. Only the least discriminatory firms survive. Indeed, if there were any firms which did not discriminate at all, these would be the only ones to survive the competitive struggle. Since in fact racial discrimination has survived for a long time, we must assume that the model just presented must have some limitation . . . .[4]

To his credit, Epstein implicitly acknowledges that any theory of discrimination needs to account for this history of discrimination. His book endeavors to provide such a theory.

Put simply, Epstein argues that freedom of contract never had a chance: prior to 1964, state law *required* employers to discriminate against blacks;[5] after 1964, Title VII prohibited discrimination. Had state governments been willing to protect businesses that hired and dealt with blacks, Epstein believes, unprejudiced entrepreneurs would have efficiently served the needs of the black community. This historical interpretation forms the very foundation of the book's larger free-market thesis: by arguing that our pre-1964 history of

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3. Gary S. Becker, The Economics of Discrimination (2d ed. 1971).

4. *See* Kenneth J. Arrow, *The Theory of Discrimination, in* Discrimination in Labor Markets 3, 10 (Orley Ashenfelter & Albert Rees eds., 1973).

5. Epstein's historical thesis extends the argument of Jennifer Roback, *Southern Labor Law in the Jim Crow Era: Exploitative or Competitive?*, 51 U. Chi. L. Rev. 1161 (1984), *reprinted in Labor Law and the Employment Market* 217 (Richard A. Epstein & Jeffrey Paul eds., 1985). Roback's thesis was:

> [Jim Crow laws governing employment] can best be understood as attempts to enforce a labor-market cartel among white employers that could not be enforced in any other way. The planters wanted to collude to hold down black wages, both to increase their own profits and to solidify the dominant position of the white race . . . . The laws were intended to accomplish what race prejudice could not do by itself.

Id. at 1162. Epstein's contribution is primarily in realizing that this argument could respond to the deficiency of Gary Becker's model in failing to account for our history of discrimination.

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racial exclusion emanates solely from state action, Epstein summarily rejects the alternative explanation that private bigotry wrought a devastating injury upon African Americans.

While Epstein is to be commended for taking history more seriously than other economists, his falsifiable theory is in this instance falsified. But in our rush to reject Epstein's hypothesis it is important that we also treat history seriously. In a recent review of Epstein's book,[6] I criticized Epstein's argument in part by arguing that Jim Crow laws "rarely placed restrictions on employers." This statement was incorrect.

Since my review appeared, I have found evidence suggesting that several Southern states, until the beginning of World War II, had laws restricting the employment opportunities of African Americans.[7] For example, in several Southern states it was a crime for an employer to entice workers away from another employer — and prosecutions for this crime of "enticement" were disproportionately used to prevent Southern planters from competing for black laborers.[8]

I imagine that some people at this Symposium will be so intent in refuting Epstein's historical thesis that they will argue that these laws merely reflected the underlying private hatred. While I believe that the laws were a reflection, they did not *merely* reflect. Jim Crow laws hurt African Americans by putting the Leviathan's coercive central power in the hands of private bigotry.

Nevertheless, this admission (that Jim Crow hurt blacks' employment opportunities) is much different from Epstein's argument that freedom of contract would have eliminated *all* invidious effects of private bigotry. As I said in my original review,

> [Epstein's] claim that prejudice and bigotry wouldn't have affected the economic opportunities of blacks (if private contracts had been respected) is surreal. Jim Crow and indirect coercion were largely confined to Southern states, but patterns of racial (and sexual) exclusion pervaded many parts of the country. Even in the South, boycotts by bigoted employers and consumers could massively restrict the profitability of integrated or all-black production.[9]

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6. Ian Ayres, *Price and Prejudice*, THE NEW REPUBLIC, July 6, 1992, at 30, 31.

7. William Cohen, *Negro Involuntary Servitude in the South, 1865-1940: A Preliminary Analysis*, 42 J. HIST. 31 (1976). I thank Lawrence Friedman for bringing this work to my attention.

8. *See id.*; Roback, *supra* note 5; Richard Sutch & Roger Ranson, *The Ex-Slave in the Post-Bellum South: A Study of the Economic Impact of Racism in a Market Environment*, 33 J. ECON. HIST. 131 (1973).

9. Ayres, *supra* note 6, at 31. John Donohue does an excellent job of falsifying Epstein's historical claim:

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Both private bigotry and public laws hurt the economic opportunities of black workers. Thus, even if the states had respected freedom of contract before Title VII, private bigotry would have dramatically restricted the economic opportunities of African Americans.

When Epstein describes his ideal of contractual freedom, he often evokes the image of a minimalist government — one that only enforces contracts (and controls the use of force and fraud).[10] In 1964, however, the costs of enforcing such contracts would have been anything but minimal. Private resistance to integration (by the KKK and others) would have made it virtually impossible for the state to commit to enforcing private contracts — recall, for example, the difficulty that federal authorities had in protecting the Selma marchers.

A vital component of Epstein's free-market theory is the existence of a profit incentive to enter markets where inefficient discrimination exists. Competition, however, will fail to eradicate bigotry if there is no "first mover" advantage to employing and/or serving the black community. It is doubtful that anyone would wish to be the first on their block to break the color barrier, because doing so would create an easy target for reactionary violence that could not be deterred without massive government expenditures.

Social acceptance of racial hatred has arguably declined in recent years, thereby making it easier to enforce a freedom of contract regime today. This suggests that today it would be harder for groups like the KKK to effectively mobilize in the face of entrepreneurial integration. Viewed in this sense, followers of Epstein could more reasonably argue that competition under a freedom of contract regime might now eliminate the harmful effects of discrimination.

Let me be clear. I believe that allowing employers to discriminate intentionally on the basis of race would hurt African Americans today, but that this damaging effect would probably be smaller than in the past. For example, changing Title VII from an immutable rule to merely a default rule would harm protected workers, but the injury would be smaller in 1993 than in 1964.[11] A default-rule version of Title VII might imply a warrantee of nondiscrimination, which an employer could only waive by explicitly disclosing to employees and

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> If one accepts the view that segregationist legislation caused the exclusion of blacks from the Southern textile industry, three conclusions follow: (1) the exclusion would not be found prior to passage of the segregationist law . . .; (2) the exclusion would occur only in areas subject to such legislation; and (3) competitive pressures would undermine the racial exclusion shortly after the unconstitutionality of the segregationist law was perceived. Yet, the evidence seems to contradict all three points.

Donohue, *supra* note 2, at 1594.

10. EPSTEIN, *supra* note 1, at 19.

11. *See* Ian Ayres & Rob Gertner, *Filling Gaps in Incomplete Contracts: An Economic Theory of Default Rules*, 99 YALE L.J. 87 (1989).

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consumers that it retains the right to discriminate on the basis of race.[12] It is likely that in 1964, many employers in both the North and the South might have routinely (and proudly) contracted around such an implied warrantee — leaving black workers with little added protection. Indeed, many public accommodations of the time openly advertized their race discrimination ("whites only"). Today, however, the social and economic costs of affirmatively contracting for the right to discriminate might be sufficient to deter many employers from opting out of potential Title VII liability.[13]

Although Epstein argues for the repeal of Title VII, he should be completely content with changing it from an immutable rule to a default rule. *Forbidden Grounds* implicitly favors an "opt-in" regime where employers would have to affirmatively warrant their intention not to discriminate. But Epstein nowhere explains why an opt-in regime is superior to an opt-out regime in which the default employment contract included an implied warranty against discrimination. I predict that many fewer employees would be covered under Epstein's opt-in proposal than under a proposal where employers had to explicitly opt out. To be sure, some establishments would contract to discriminate regardless of the default. But even if immutability is less important in 1993, default choice is more important.

Epstein's analysis of history attempts to move beyond prior economic theories of discrimination that largely ignore the failure of competition to drive out discrimination. Despite this strength, his conclusion that competition and contractual freedom could have significantly expanded the economic opportunities of blacks is unconvincing. Because state law was not the sole force perpetuating inefficient discrimination, it seems unlikely that conditions in 1964 would have permitted a minimalist freedom of contract approach. The most important benefit of Epstein's analysis may be to force us to grapple with the likely consequences of contractual freedom in

12. *See* Ian Ayres, *Fair Driving: Gender and Race Discrimination in Retail Car Negotiations*, 104 HARV. L. REV. 817, 867 (1991) ("Following the *Patterson* rationale, finding an implicit representation not to treat consumers differently in bargaining because of the race or gender would offer a free market alternative to civil rights interventionism."); DERRICK BELL, FACES AT THE BOTTOM OF THE WELL: THE PERMANENCE OF RACISM 46-47 (1992) (discussing hypothetical sale of "racial preference licenses" by government to private parties).

13. Warranties that apartments will be in a livable condition or that products will be useable are routinely presumed in contract law (absent express agreement to the contrary), but under the *Forbidden Grounds*' analysis contract law would presume that employment discrimination was lawful. Epstein not only wants freedom of contract, but he wants to allow employers to avoid the discomfort of admitting when they do discriminate.

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today's market.

II. PUBLIC ACCOMMODATIONS

Epstein's analysis of history is possibly at its nadir when he tackles the implementation of Title II, barring discrimination in public accommodations. Here Epstein claims that: "The early instances of noncompliance [with Title II] *all* arose when individual firms, eager to obey the law, found themselves set upon by gangs of racists determined to shut them down by brute force."[14]

Though I do not profess to be a student of history, I find it implausible that *all* noncompliance was caused in this way. Events of the time suggest that the bigotry of owners caused at least some of the noncompliance.[15] For example, Lester Maddox gained national publicity shortly after passage of the 1964 Civil Rights Act when he distributed ax handles to supporters in order to prevent blacks from patronizing his Atlanta restaurant, the Pickrick.[16] Maddox's actions are not consistent with Epstein's view that noncomplying firms were "eager to obey the law."[17] Indeed, the heinous conduct of Maddox may have not only been profit-maximizing, but it also propelled Maddox to Georgia's governor's office from 1966 until 1970.[18]

As with employment, Epstein argues that state interference with freedom of contract prevented the market from providing adequate eating and sleeping accommodations for African Americans. But he again fails to provide any convincing evidence that the state laws were the "but for" cause of this failure. He confidently asserts:

> Someone could have made a fortune catering solely to blacks who were kept out of the white hotels that adopted segregationist policies. Yet . . . [n]o firm could have entered the market in the face of the political forces that were arrayed against it. The dog that did not bark gives the best evidence of pervasive government involvement in this area.[19]

Epstein's confidence seems misplaced. While government involvement might conceivably deter an entrepreneurial entrant, the failure

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14. EPSTEIN, *supra* note 1, at 127 (emphasis added).

15. Even today there are reports of explicit racial discrimination at public accomodations that do not seem to be caused by private coercion. *See* Lynne Duke, *More Denny's Patrons Allege Racial Bias; Several Incidents Reported in 5 States*, THE WASH. POST, June 17, 1993, at A20.

16. *Ex-Governor Lester Maddox of Georgia has Heart Surgery*, REUTERS, Apr. 1, 1991; *Maddox to Campaign in Carolinas Against Dukakis*, UPI, Oct. 17, 1988.

17. EPSTEIN, *supra* note 1, at 127. It is possible that Epstein just misspoke in making this assertion. Earlier in the same paragraph he admits that "our most dramatic recollections about the enforcement of Title II in 1964 revolve around the few establishments that defied the law." *Id.*

18. Maddox defeated Jimmy Carter for the Democratic gubernatorial nomination in 1966 and later served as lieutenant governor under Carter from 1971-75. *See* REUTERS, *supra* note 16.

19. EPSTEIN, *supra* note 1, at 127.

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of entrepeneurs to attempt entry is equally consistent with the hypothesis that there was not a fortune to be made without the patronage of prejudiced customers.

III. HOUSING

Epstein's only reference to our prohibition against race discrimination in the housing market is his criticism of a 1988 amendment making it illegal for rental, condominium and cooperative units to discriminate against families with children.[20] Epstein argues that this amendment "struck genuine fear into the hearts of many older residents . . . who just do not want to have children around."[21] Although Epstein only addresses the "families with children" provisions of the Fair Housing Act, the thrust of his libertarian argument surely suggests that it too should be repealed.

Conspicuous by its absence is any discussion of race discrimination in housing markets. Epstein conveniently ignores the pervasive evidence of past and present racial exclusion in real estate sales and rentals throughout the country.[22] Epstein cannot plausibly argue that the restricted housing opportunities of African Americans are due solely to legally mandated discrimination or some other statistical theory.

Admittedly, state and local laws injured blacks' housing opportunities. Several cities, for example, established zoning ordinances which mandated segregated housing;[23] even the Federal Housing Administration established appraisal policies which flatly asserted that integration of all white neighborhoods had a "value-destroying tendency."[24] However, as Gunnar Myrdal concluded in *An American Dilemma*: "Probably the chief force maintaining residential segregation of Negroes has been *informal* social pressure from the whites. Few white property owners in white neighborhoods would

20. *See* Fair Housing Amendment Act of 1988, Pub. L. No. 100-430, § 805(d), 102 Stat. 1619, 1621.

21. EPSTEIN, *supra* note 1, at 64.

22. *See, e.g.*, George Galster, *More Than Skin Deep: The Effect of Housing Discrimination on the Extent and Pattern of Racial Residential Segregation in the United States*, *in* HOUSING DESEGREGATION AND FEDERAL POLICY 119 (John M. Goering ed., 1986); Douglas S. Massey & Nancy A. Denton, *Trends in the Residential Segregation of Blacks, Hispanics, and Asians: 1970-1980*, 52 AM. SOC. REV. 802 (1987); John Yinger, *Measuring Racial Discrimination with Fair Housing Audits: Caught in the Act*, 76 AM. ECON. REV. 881 (1986).

23. GUNNAR MYRDAL, AN AMERICAN DILEMMA: THE NEGRO PROBLEM AND MODERN DEMOCRACY 623 (1962).

24. DAVIS MCENTIRE, RESIDENCE AND RACE 160 (1960).

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ever consider selling or renting to Negroes."[25] The clearest evidence that laws mandating discrimination were insufficient to achieve their purpose was the wide-spread use of restrictive covenants — prohibiting the sale or rental to various racial and religious groups.

Epstein might want to argue that the Fair Housing Act should not be repealed (even though Title VII should) because housing markets are not as competitive as are markets for labor. But in other writings, Epstein repeatedly asserts that the market for housing is presumptively competitive.[26] The housing market clearly has had a chance, but has failed to produce equal racial opportunities. The passage of the Act has not been sufficient to eliminate the persistence of disparate treatment[27] — even though the United States has an extremely competitive market where voluntary contracts are by and large enforced. Private refusals to deal and contractual commitments to discriminate have massively restricted the housing opportunities of African Americans, but these harms must be countenanced by Epstein's libertarian analysis.

Indeed, from his other writings it seems that Epstein would be willing to protect the right of property owners to contractually commit to racially restrictive covenants. In a 1988 article entitled *Covenants and Constitutions*,[28] Epstein addressed the enforceability of covenants that mandate discrimination:

> Restrictive covenants have also been used to exclude persons from real estate developments because of their race or religion. As a matter of American constitutional and statutory law, these covenants are now universally regarded as illegal, precisely because of their adverse effects on third parties. My purpose here is not to assess the desirability of constitutional rules or statutes but only to stress again the general point. *Any concern with antidiscrimination is best attacked head on and does not raise any problems with restrictive covenants that are not also found, say, with employment or with housing generally.* It is very doubtful, therefore, that any distinctive doctrine of covenant law can begin to reach this issue. Restrictive covenants of this sort touch and concern the land, are negative in effect, and clear as to both intent and meaning, and are capable of recordation. Yet all this only shows that the problem is better handled by other legal rules which have discrimination, race, and religion at their core, and not by

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25. MYRDAL, *supra* note 23, at 622.

26. Richard A. Epstein, *Rent Control and the Theory of Efficient Regulation*, 54 BROOK. L. REV. 741, 762 (1988); Richard A. Epstein, *Rent Control Revisited: One Reply to Seven Critics*, 54 BROOK. L. REV. 1281, 1286 (1988) [hereinafter *Rent Control*] ("All competition requires is many buyers and many sellers in a market of free entry. Housing rental markets easily satisfy that definition.").

27. The open nature of this discrimination was recently dramatized by ABC's PrimeTime Live program "True Colors." Hidden cameras captured the disparate treatment of a black male and white male. Donohue, *supra* note 2, at 1608-09, also discusses the program. The power of this visual proof supplements the massive body of fair housing audits conducted since the passage of Title VII. *See* Yinger, *supra* note 22.

28. Richard A. Epstein, *Covenants and Constitutions*, 73 CORNELL L. REV. 906 (1988) [hereinafter *Covenants and Constitutions*].

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the law of covenants.[29]

Although Epstein states in this article that his purpose "is not to assess the desirability" of antidiscrimination provisions,[30] it is clear that his purpose in *Forbidden Grounds* is to demonstrate that such provisions are not desirable. He admits that "[a]ny concern with anti-discrimination . . . does not raise any problems with restrictive covenants that are not also found, say with employment." Given his views about employment discrimination, one can deduce that Epstein believes restrictive covenants mandating racial and religious exclusion should be enforced.[31]

The only unclear issue is whether Epstein would argue that the existing restrictive covenants should spring back into force.[32] These covenants are still recorded and routinely included in closing documents. Epstein might argue that many current owners have, in purchasing, relied on the nonenforcement of these covenants. But as long as they purchased the land with notice that such covenants exist, at least some authors have argued that they have purchased with the knowledge that the covenants may spring back into force and have (effectively) assumed this risk.[33]

Before neutrally assessing this issue, we might want to consult our own deeds. Gunnar Myrdal, for example cites evidence that, Circa 1940, 80 percent of Chicago was covered by such restrictive covenants.[34] I wonder what proportion of this audience might have to sell their houses and move if we were to suddenly begin enforcing these voluntary contractual provisions.

My goal here is to clarify Professor Epstein's position. As a normative matter:

A. Should we repeal all of the Fair Housing Act?; and

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29. *Id.* at 918 (emphasis added); *see also* Richard A. Epstein, *Notice and Freedom of Contract in the Law of Servitudes*, 55 S. CAL. L. REV. 1353 (1982).

30. *Covenants and Constitutions*, *supra* note 28, at 918.

31. I draw this conclusion because Epstein believes that there should not be any "distinctive doctrine of covenant law" and because he argues that "restrictive covenants of this sort" have all the required indicia of enforcement — that is, they "touch and concern the land, are negative in effect, are clear as to both intent and meaning, and are capable of recordation." *Id.* at 919.

32. An analogous issue concerns whether antiabortion laws that have been held to be unconstitutional under Roe v. Wade, 410 U.S. 113 (1973), and its progeny would spring back into effect if the Supreme Court were to overrule *Roe*. *See, e.g.*, GUIDO CALABRESI, A COMMON LAW IN THE AGE OF STATUTES (1982) (arguing that common law courts have power to invalidate statutes on grounds of desuetude).

33. Louis Kaplow, *An Economic Analysis of Legal Transitions*, 99 HARV. L. REV. 509, 511 (1986).

34. MYRDAL, *supra* note 23, at 624.

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B. Should preexisting covenants spring back to life?

Epstein's answer to the first question surely must be in the affirmative. If Epstein's argument is to be consistent with his past views, he is forced to argue that government should have only (1) struck down the laws that mandated housing discrimination and (2) eliminated the violence and intimidation that interfered with the freedom to sell and lease property. I agree with Professor Epstein that these are laudable goals.

I am completely unconvinced, however, that refusals to deal and restrictive covenants would not have continued to wreak havoc on the housing opportunities of people who are currently protected by the Fair Housing Act. Both refusals to deal and restrictive covenants (which mandate such refusals) would be absolutely unregulated under Epstein's analysis. While I agree that striking down Jim Crow laws and eradicating private violence would improve the housing opportunities of blacks, I do not believe that free market competition would eliminate the impact of racist preferences.

My inference that Epstein should favor the repeal of the Fair Housing Act has the sound of a dramatic accusation — and Epstein could undermine the need for all this labored analysis by saying: "Of course the Fair Housing Act should be repealed; segregated housing is efficient." But if this is true, why did *Forbidden Grounds* only criticize the Act's prohibition of housing discrimination against families with children? The title of the book notwithstanding, it seems that the market for real property is a ground on which Epstein is reluctant to tread.

IV. AUTOMOBILES

Epstein spends four pages critiquing a recent study of mine that tested for race and gender discrimination in new car sales.[35] At the risk of boring the audience, I would like to offer a few thoughts in response. In my study, more than 180 independent negotiations at ninety dealerships were conducted in the Chicago area to examine how dealerships bargain. Testers of different races and genders entered new car dealerships separately and bargained to buy a new car using a uniform negotiation strategy.[36] Epstein does a capable job summarizing the controls:

> The testers chosen were carefully controlled so as to appear to come from the same young, educated professional class living in the same appropriate neighborhoods; each buyer was instructed to express an interest in the same car, and to indicate a willingness to provide private financing. All potential buyers used the same bargaining strategy: buyers first obtained an offer

35. *See* EPSTEIN, *supra* note 1, at 51-54 (critiquing Ayres, *supra* note 12).
36. Ayres, *supra* note 12, at 818.

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> from the dealer's representative and then made a counteroffer that indicated knowledge of the dealer's cost; thereafter the subject offered a price that split the difference between his or her original offer and the last offer received from the salesperson. The experiment continued until the sales representative refused to bargain or "attempted" to accept the last offer made by the subject.[37]

At first glance, one might think that car bargaining provides an ideal setting to test Epstein's free market hypothesis. Certainly, it is difficult to argue that the government mandates discrimination in this market or that law enforcement turns a blind eye toward private harassment of nondiscriminating sellers. Moreover, the market amply fulfills Epstein's requirements for competition: "All competition requires is many buyers and many sellers in a market of free entry."[38] Consequently, one would expect the power of market competition to eradicate any embarrassing effects of race or gender discrimination.

However, after reading Epstein's analysis I come away wondering whether his theories are susceptible to embarrassment — known in more conventional economic terms as falsifiability. As an initial matter Epstein is not fazed by the raw evidence that dealerships charge dramatically higher prices to black and/or female testers than to white male testers. As reported in my initial study,[39] the average dealer profits for final offers made to different classes of testers were:

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37. EPSTEIN, *supra* note 1, at 51; *see also* Ayres, *supra* note 12, at 822. For the record, Epstein mistakenly says that the testers were students. EPSTEIN, *supra* note 1, at 51. Virtually all of the testers were hired from people responding to newspaper ads — only a small proportion were currently students. I also fail to understand why the word "attempted" is placed in quotations in the foregoing quotation. But these are inconsequential quibbles.

38. *Rent Control*, *supra* note 26, at 1286.

39. A follow-up study using 38 testers bargaining for more than 400 cars at more than 240 dealers substantially confirms these results. In this larger data set, sellers systematically offered lower prices to white male testers. The offers to other tester groups exceeded the offers to white males by the following amounts: white females $244; black female $457; and black male $1288. Ian Ayres & Peter Siegelman, *Race and Gender Discrimination in Bargaining for a New Car*, AM. ECON. REV. (forthcoming 1994). In the additional testing, black males fared worse than black females. As I noted in the original study:

> This suggests that individual characteristics of the testers may have influenced the results. The black male tester in the initial experiment, for example was himself a former car salesperson and is currently a law student. It is possible that the lower offers he received in the initial experiment were by-products of his overly aggressive deviations from the script.

Ayres, *supra* note 12, at 828 n.36. In the follow-up study, we tested for the presence of individual tester effects using a "fixed-effects" specification and found no evidence of individual effects among our larger group of 38 testers.

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White Male	$ 362
White Female	$ 504
Black Male	$ 783
Black Female	$1,283

After restating these results, Epstein reasonably asserts: "The critical question is how to interpret these results."[40] But at this point, Epstein's analysis becomes less clear. He avers at least indirectly to some five different potential explanations for these results — but never clearly says whether any of these explanations might cut against his theories. Indeed, I find myself wondering what kind of evidence could ever falsify Epstein's theories. To aid in the analysis, I will try to divide his analysis into its five constituent parts.

1. *Lack of Sufficient Control.* Epstein begins with the standard observation that these differences in final offers do not constitute race and gender discrimination if the testers' behavior or appearance differed:

> Although Ayres tried to control for all relevant variables, there has to be a sense in which he failed. He notes that his subjects were instructed to say that they were able to provide independent financing; yet sales personnel continued to ask questions about car financing (most often of black females), perhaps because they regarded any customer statement about financing as a ploy that could not be believed uncritically.[41]

While I agree with Epstein that it is impossible to precisely control all dimensions of bargaining conduct,[42] his analysis of this point is inapposite. The tendency of sales personnel to question the testers' assertion that financing was unnecessary does not prove that the testers were nonuniform. It only indicates that the salespeople tended to discredit the uniform assertion. Further, the higher tendency to question the assertions of black females does not prove that the testers bargained in a nonuniform manner: it may only indicate that the salespeople made statistical inferences about the likelihood that the uniform assertion was false based upon the tester's race and/or gender.

To his credit, Epstein acknowledges that "[i]t is unlikely that

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40. EPSTEIN, *supra* note 1, at 52.

41. *Id.*

42. Indeed, in the original article I concluded the methodology section by admitting:

> Despite these attempts to control for uniform tester behavior, at some level of abstraction the non-verbal behavior of the testers must have inevitably diverged. Salespeople may have offered certain testers a higher price not because of their race or gender, but because they blinked more often or opened the car door more quickly.

Ayres, *supra* note 12, at 826.

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these hidden difficulties [concerning whether the testers were adequately controlled] account for all the differentials that were reported."[43] This is not a trivial concession, as it implies that Epstein acknowledges the existence of systematic race and gender discrimination — at least for buyers who adopt this bargaining strategy. However, an acknowledgement of race discrimination is not an acknowledgement of an embarrassing market failure.

2. *Cost-Based Discrimination.* For Epstein, the least embarrassing explanation for race discrimination concerns cost-based differences. If dealers charge black testers more, because black consumers are on average more costly to deal with — Epstein would consider the dealer's higher offers to black customers to be completely justified. The essence of Epstein's argument is that if sellers "believed there was more a chance that the deal [with a black tester] would fall through," the sellers might be induced "to charge higher prices to cover their own cost."[44]

It is not clear, however, that the belief of a high probability of bargaining failure will cause a profit-maximizing seller to demand a high price. For example, it might be more worthwhile for the seller to start with a lower offer in such instances, thereby avoiding the expense of bargaining over multiple periods. Indeed, many game-theoretic bargain models suggest that a higher probability of bargaining breakdown will induce lower seller offers.[45] Consistent with this finding, Peter Siegelman and I have recently estimated the exogenous probability of the deal falling through (implied from the sellers' behavior). We found that sellers act as if the probability of breakdown is much lower in negotiations concerning black males than white males.[46] Thus Epstein's analysis is doubly flawed: the dealers may not believe that there is a larger probability that deals with black customers will fall through; and if profit-maximizing dealers had such beliefs, it would cause them to offer lower prices — not higher prices.

Putting aside the niceties of this argument, the major point is that Epstein only claims that "some portion" of the price difference may be cost driven — suggesting that other portions of the disparate racial and gender treatment may be caused by other — and possibly

43. EPSTEIN, *supra* note 1, at 52.
44. *Id.* at 53.
45. *See, e.g.*, Peter C. Cramton, *Dynamic Bargaining with Transaction Costs*, 37 MGMT. SCI. 1221 (1991).
46. Ayres & Siegelman, *supra* note 39, at Table 5.

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more embarrassing — explanations.

3. *Revenue-based Discrimination.* Surprisingly, Epstein never directly addresses the explanation that I believe has the strongest support:[47] sellers may use race and gender proxies in order to extract more revenue from different classes of buyers: "[G]roup differences in search costs, information, and aversion to bargaining may explain why profit-maximizing dealers charge white males less."[48]

Economists refer to this notion as third-degree price discrimination. One would think that this is a slightly more embarrassing explanation. Free market competition should protect minorities from any discrimination that is wholly unrelated to the costs of doing business. Yet Epstein is completely silent about the explanatory power of revenue-based discrimination. He only indirectly engages this theory with the following comments:

> Even if one observed practice markets in which blacks and women paid higher prices than white males, each and every voluntary transaction that took place would improve the position of both buyer and seller. The only effect of discrimination here would be to change the percentage of the *surplus* from trade that is obtained by the two parties.[49]

This is one of Epstein's more labored arguments because it insulates all market failures (including monopoly overpricing) from normative criticism. Surely the welfare of those who fail to trade also counts in the efficiency analysis. Moreover, his larger argument that free market competition would give blacks the same economic opportunities of similarly situated whites fails even if the higher prices merely represent a transfer of consumer surplus to the producer.[50]

4. *Animus-based Discrimination.* Finally, Epstein misstates my conclusion on the most embarrassing explanation for discrimination — animus. If the bigotry of the customers, employees and/or owners of the dealership are the cause the dealers' disparate treatment, Epstein would be at pains to extol the a priori virtue of free market competition. Epstein writes that my "study did not reveal any form

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47. In the original study, I wrote: "Although more study is warranted, it appears that the revenue-based theory best explains the discrimination that the testers encountered." Ayres, *supra* note 12, at 845.

48. *Id.* at 849. Revenue-based discrimination may persist even in a market with multiple sellers:

> Anecdotal evidence suggests that at some dealerships up to fifty percent of the profits can be earned on just ten percent of the sales. Profit concentrations of this magnitude are crucial in understanding why competition does not eliminate revenue-based price discrimination . . . . [T]he competitive incentive to move away from bargaining to a stated-price system simply may not be compelling because dealerships would thereby lose the profits from sucker sales.

Id. at 854.

49. EPSTEIN, *supra* note 1, at 54.

50. Moreover, the greater the distortion of the price paid by blacks, the more inefficient their consumption decisions are from a social welfare standpoint — due to substitution effects.

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of discrimination attributable to the prejudices of individual sellers."[51] I, however, concluded that "[a]nimus theories find more support in the data [than cost-based theories]. The testers, for example, recorded several instances of overtly sexist and racist language by sellers."[52] Moreover, I stressed that "simple causal theories of discrimination [may] fail to capture the mutually enforcing nature of multiple causes."[53] The follow-up testing has produced additional evidence that is consistent with seller animus.[54] Although revenue-based discrimination remains the best explanatory theory, it is wrong to say that the study does not reveal any evidence of animus.

5. *Private and Public Remedies.* Epstein also criticizes the relevance of the study by suggesting that private parties are better equipped to circumvent the effects of discrimination than are public efforts. The first argument is that even if the observed discrimination were objectionable, buyers could "adopt some strategies that will reduce the variation to below that observed in Ayres' experimental study."[55] For example, Epstein argues: "If blacks or women know that they are apt to get a good deal from some small fraction of the market, then they can avoid other, less receptive dealerships and their unattractive offers."[56] This is an internally consistent theory. It is however highly implausible. I could not econometrically identify any dealership characteristics that were correlated with the level of discrimination. The forms of race and gender discrimination were strikingly similar across different types of dealerships.[57] Moreover, ask yourself whether you have any idea about which dealers in your city give the best deals (to people of your race and gender).

More plausibly, Epstein argues that the observed discrimination might have been smaller if black and/or female testers had brought along a friend or elicited a rival offer from a rival dealership.[58] The

51. EPSTEIN, *supra* note 1, at 53-54.
52. Ayres, *supra* note 12, at 846.
53. *Id.* at 852.
54. For example, there is some empirical evidence that the sellers' bargaining strategy with black male testers was influenced by "consequential animus" — i.e., the sellers gained added pleasure from gaining an extra dollar from a black male customer. *See* Ayres & Siegelman, *supra* note 39.
55. EPSTEIN, *supra* note 1, at 53.
56. *Id.* at 52.
57. This result tends to undercut the hypothesis that the disparate treatment is due to certain kinds of animus. One would expect to find varying degrees of animus at different locations.
58. EPSTEIN, *supra* note 1, at 52. However, Epstein misstates my results in arguing that insisting on a test drive could induce lower offers. He reports that in my study insisting on a test drive "was found to lower the final offer by $319[]." *Id.* That was not

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possibility that nonwhite male testers could reduce the amount of discrimination by employing these strategies, however, is undermined by anecdotal evidence that race and gender discrimination may be so ingrained in a dealership's behavior that it is hard to overcome with simple strategies. For example, I offered a group of research assistants a monetary prize if they could obtain a better deal in no-holds-barred bargaining. My assistants were approximately my age, highly educated and had been studying the car market. This contest's incentives did produce lower seller offers, but significant amounts of discrimination remained: the black male and black female best offers were more than $700 dollars higher than the best offer that I received as a white male.[59]

Even if black testers could get a better deal by bringing along a friend or visiting additional dealerships, the study still reveals an important aspect of race discrimination because the white male testers did not have to go to the trouble of undertaking the additional costs of these counter-strategies. Perhaps the black and female testers could have received the white male price if they had executed twenty push-ups during the course of bargaining. The discriminatory effect is found in the fact that the white male testers did not need to execute the push-ups to secure a low price.

Epstein even uses the likely resistance of black and female consumers to criticize the ability of audit methodologies to measure discrimination: "[I]t is most likely that blacks and women tend to reject the worst dealer offers, so any observed price disparity is likely to be smaller than those obtained by the simulation."[60] As with his analysis of the efficiency of price discrimination, Epstein ignores the fact that significant social costs of discrimination are created from those who fail to buy. In the housing context, certainly those buyers who are unable to buy because sellers refuse to deal or refuse to offer a reasonable price represent cognizable victims of discrimination. However, Epstein would not include such buyers in his social welfare calculus because they do not trade at an "observed price disparity."

The practice of marginalizing the consumers who are rationed out of the market is particularly important because in more than 70 percent of the observations in my data, the dealer ultimately refused to bargain further (when tester was last to concede). Epstein chooses to

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my result. Instead, the study found "revealing that a tester *had already taken* a test drive reduced the seller's final offer by $319. . . . Testers that provided dealers with explicit evidence of competition (by revealing a prior test drive) received significantly better deals." Ayres, *supra* note 12, at 848-49 (emphasis added).

59. Additional details of this "beat-the-boss" test can be found in Ayres, *supra* note 12, at 828-29 n.36.

60. EPSTEIN, *supra* note 1, at 53.

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describe this outcome as "final offers that were rejected by . . . testers"[61] — but all testers showed an equal willingness to continue making concessions as long as the dealership was. Tests ended either when the dealership refused to make further concessions or when the dealership attempted to accept one of the tester's concessions. The dealership's unwillingness to make further concessions was particularly frequent with nonwhite male testers. When the tester was a white male, 25.6 percent of the tests ended in attempted seller acceptances; however, this figure fell to 14.9 percent for the other tester types.[62] Contrary to Epstein's analysis, the fact that sellers are more likely to accept offers from white males actually biases our estimates *against* finding discrimination, however, since dealership acceptances only provide an upper bound for the sellers' reservation price. That is, in those cases where dealers attempted to accept an offer from a white male tester, the dealers might have been willing to make an even lower offer, which would have increased our measure of discrimination. Epstein's conclusion that "the level of disparity observed in any test will be greater than that found in any active market"[63] thus wrongfully ignores both the additional efforts of minority buyers and dealership refusals to bargain.

While Epstein argues that private counterstrategies could undo any embarrassing consequences of discrimination, he is pessimistic about any palliative role for government intervention, stating: "[T]here seems to be very little that can sensibly be done to change the basic situation."[64] In response to one of my suggestions that dealerships might be required to reveal the average price for which each make of car is sold or the size of the markup on an individual transaction, Epstein responds that "a regulation of that sort would doubtless wreak havoc with the traditional system of commission compensation for car sellers, and would reduce their incentive to close sales."[65] I normally agree that we should be reluctant to adopt regulations that intervene substantially in individual markets. But we should be less reluctant to "wreak havoc" in markets that most people in this country find so objectionable. Moreover, Epstein's conclusion concerning the incentive to close seems counter-intuitive: if

61. *Id.* at 53.
62. Ayres & Siegelman, *supra* note 39, at 13.
63. EPSTEIN, *supra* note 1, at 54.
64. *Id.*
65. *Id.*

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salespeople received a fixed amount per car, they would have increased incentives to close (because they would only increase their salary by closing more deals); under the current system, however, salespeople may very well be willing to accept a lower chance of closing some deals if they can sell the car at a substantial markup.

And of course Epstein argues by *ipse dixit* that the burden should be on interventionists to prove that regulation would improve the current equilibrium:

> It is not enough to show that there is some residual level of discrimination in a market to make the case for regulation. It has to be shown as well that the proposed cure can identify and isolate the evils in some cost-effective fashion. In light of the avenues of self-help that are available to all customers, it seems unlikely that regulation could ever accomplish a net social good.[66]

This quotation — which tends to epitomize much of Epstein's scholarship — fails to explain why the burden of persuasion should rest with those who want to eliminate discrimination. Although Epstein maintains the theoretical possibility that an empirical "showing" might justify regulation in some instances, I have the impression that no empiricism about the workings of a free market could falsify his theories to the extent that he would actually reach the second question of whether regulation could be cost-justified.

CONCLUSION

In this Article, I have tried to show that invidious forms of discrimination can persist in competitive markets even when government has not mandated disparate treatment. In the housing and automobile markets, there is strong evidence that race discrimination is not cost-justified; yet competition in these markets has failed to accomplish the goal of section 1981 that "a dollar in the hands of a Negro will purchase the same thing as a dollar in the hands of a white man."[67] In turn, this showing tends to undercut our confidence that competition would eradicate invidious discrimination in employment.

In concluding, let me turn to a public choice criticism of *Forbidden Grounds*. I continue to be amazed that Epstein, of all people, offers no explanation for the tremendously broad base of support for Title VII. Indeed, the book's introduction, entitled "Consensus and its Perils," turns Epstein's own libertarian ideology on its head. Libertarians usually argue that individuals' preferences are the only knowable indicators of value, but Epstein, for some reason, discounts

66. *Id.*
67. Jones v. Alfred H. Mayer Co., 392 U.S. 409, 443 (1968).

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personal preferences when it comes to our civil rights laws. He admits that there is incredibly pervasive support for the notion that employers should not be allowed to discriminate on the basis of race, but this support contradicts his theory that our civil rights laws hurt not only whites but the vast majority of blacks. Epstein "proves" that integration hurt some blacks because the owners of black baseball teams lost the value of their franchise when the major leagues integrated — but even here I would bet that some of the owners supported integration.

I once asked Professor Epstein, after a presentation at the University of Virginia, why virtually all African Americans supported Title VII if the legislation injured them. Epstein's answer (to the best of my memory) was two-fold. First, a small number of blacks are helped by Title VII and these people control the lobbying organizations (such as the NAACP) which speak for their entire race. Second, Epstein argued that the larger group of blacks (who are hurt by Title VII) face enormous social pressures not to dissent. To his credit, these explanations do not turn on false consciousness or irrationality. As a libertarian Epstein cannot admit the possibility of false consciousness without destroying the analytic power of revealed preference theory and freedom of contract.

However, in admitting that black people are subject to powerful social pressure, Epstein fails to appreciate how analogous forms of social pressure might also distort the behavior of white people. If Epstein is to be consistent, he should either retreat from the claim that social pressure prevents the majority of blacks from opposing Title VII or admit that the same type of social pressures could affect the behavior of white entrepreneurs. In essence, Epstein cannot have it both ways. Nonlegal pressures cannot distort the choices of blacks, yet fail to distort the choices of other market participants.

Finally, I believe that one of the book's biggest shortcomings is Epstein's failure to admit the empirically contingent nature of his arguments. This is a criticism that is often levelled at law and economics scholarship, but it is not a necessary attribute. For instance, Frank Easterbrook and Dan Fischel do a much better job of stressing empirical ambiguities and indicating when choice of efficient law will turn on underlying facts.[68]

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68. *See* FRANK H. EASTERBROOK & DANIEL R. FISCHEL, THE ECONOMIC STRUCTURE OF CORPORATE LAW 314 (1991) (for example, in analyzing mandatory disclosure rules in securities laws, authors refreshingly admit "[w]e are left, for the moment at least, with arguments rather than proof"); *see also* Ian Ayres, *Making a Difference: The*

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Epstein's willingness to make unqualified assertions belies his nonempirical orientation. Earlier in this Article, I criticized Epstein's implausible claim that "the early instances of noncompliance [with Title II] *all* arose when individual firms eager to obey the law found themselves set upon by gangs of racists . . ." (emphasis added)[69] Epstein makes a similarly implausible absolute in his concluding chapter: "Anyone who works in academic circles, and I dare say elsewhere, knows full well that *all* the overt and institutional discrimination comes from those who claim to be the victims of discrimination imposed by others."[70] I find several aspects of this claim to be patently false. First, Epstein's claim that all the discrimination "comes from" those who claim to be victims is clearly wrong if he means that it is *caused by* blacks and women. White males constitute the voting majority at virtually every law school in the country[71] and most other academic departments. Thus, it is misleading to say that discrimination "comes from" women and/or minorities.

But regardless of cause, it is indefensible to assert that *all* overt and institutional discrimination is in favor of women and minorities. Let me offer a personal counter example. I am the beneficiary of overt institutional gender discrimination — in that I was given a nearly full scholarship to Yale Law School because I am male.[72] I received a Victor Wilson scholarship that is only given to males from Kansas City, Missouri. The Supreme Court of Missouri expressly refused to enjoin the exclusion of women by the trust document.[73] I can honestly say that without this scholarship I would probably not have attended Yale Law School and may very well have taken a different career path. I believe that other professors could provide many more serious instances of overt discrimination.

So in closing, let me adopt a rhetorical device that Al Gore used repeatedly in debating Dan Quayle. I do not realistically hope to change Professor Epstein's belief that Title VII should be repealed — but I hope that he would rethink a few of his statements. Just as I have conceded that I was wrong in claiming that Jim Crow laws

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Contractual Contributions of Easterbrook and Fischel, 59 U. CHI. L. REV. 1391 (1992) (reviewing FRANK H. EASTERBROOK & DANIEL R. FISCHEL, THE ECONOMIC STRUCTURE OF CORPORATE LAW (1991)).

69. *See supra* p. 7.

70. EPSTEIN, *supra* note 1, at 503.

71. *See* Robert J. Borthwick & Jordan R. Schau, Note, *Gatekeepers of the Profession: An Empirical Profile of the Nation's Law Professors*, 25 U. MICH. J.L. REF. 191, 200 (1991).

72. Some readers may notice the relation to Steve Carter's story of applying to law school. STEPHEN L. CARTER, REFLECTIONS OF AN AFFIRMATIVE ACTION BABY (1991).

73. Shapiro v. Columbia Union Nat'l Bank & Trust Co., 576 S.W.2d 310, 312 (Mo. 1978) (en banc), *cert. denied*, 444 U.S. 831 (1979) (administration of trust does not rise to level of "state action" in violation of equal protection clause of fourteenth amendment).

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"rarely placed restrictions on employers," I hope that Professor Epstein will now concede that (1) at least some of the resistance to Title II was not by firms "eager to obey the law"; and (2) at least some of the overt and institutional discrimination in academics continues to be against the traditional victims of discrimination. In making these concession, Epstein would be moving toward the empirical grounds where the ongoing debate over many aspects of our civil rights laws should take place.

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