# Introduction

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# DOES LAW MATTER? AN INTRODUCTION

*Michael Faure*
*Jan Smits*


FACULTY OF LAW
MAASTRICHT UNIVERSITY

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Michael Faure, Maastricht University and Erasmus University Rotterdam
michael.faure@maastrichtuniversity.nl

Jan Smits, Maastricht University and University of Helsinki
jan.smits@maastrichtuniversity.nl

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*Abstract*

This contribution addresses the importance of institutions for economic development and in particular the role of law for economic growth. It was written as the introduction to an edited volume that critically considers the so-called legal origins-thesis. This thesis claims that the economic performance of a country is largely the result of that country's legal system and in particular of how this legal system has come about. Economic indicators would show that in particular common law countries are better suited to meet the interests of business than civil law countries. This volume takes stock of the debate by offering a multi-disciplinary approach to the relationship between legal rules and economic growth. It contains a general part with theoretical, empirical, historical and economic analysis of the legal origins-claim, a part on differences among various jurisdictions (including China) and a part on specific fields of law (including discussion of corporate law, property law and environmental law).

*Keywords*: Legal origins; economic growth; comparative law; economic analysis; China

# DOES LAW MATTER? AN INTRODUCTION*

MICHAEL FAURE & JAN SMITS

## 1. Increasing Relevance

This book[1] addresses the importance of institutions in economic development and in particular the role of law for economic growth. There are at least three different reasons why this topic is increasingly relevant from both an academic and a practical perspective.

First, we have seen in the last fifteen years the emergence of a strong economic scholarship pointing at the importance of law for economic development. This literature suggests not only that law is highly relevant in the development of countries, but also that particular legal systems do better than others. Thus, the so-called legal origins-thesis claims that the economic performance of a country is largely the result of that country's legal system and in particular of how this legal system has come about. Economic indicators would show that in particular common law countries are economically more developed, or at least better suited to the interests of business, than civil law countries.[2] According to this thesis, the main explanation for this phenomenon would lie in the fact that civil law countries are more geared towards State intervention whereas common law countries better facilitate the market economy.[3]

This legal origins-thesis was developed in a number of articles by economists Rafael La Porta, Andrei Shleifer and others.[4] Their original thesis was limited to the field of corporate governance, showing that if legal rules on protection of investors (shareholders) are measured, they show differences that correlate systematically with the legal traditions in which these rules find their origins, common law countries being more protective of shareholders than civil law countries.[5] In later studies, La Porta *et al.* broadened their thesis to other fields, claiming that legal origins could also explain differences among legal systems in the fields of e.g. banking, labour

* Published in: Michael Faure & Jan Smits (eds.), Does Law Matter? On Law and Economic Growth, Cambridge-Antwerp (Intersentia) 2011, pp. 1-18.

1 Michael Faure & Jan Smits (eds.), *Does Law Matter? On Law and Economic Growth*, Cambridge-Antwerp 2011.

2 This claim as such is not entirely new. Already in the first edition (1972) of Posner 2011 the argument is made that many doctrines of the common law induce efficient behaviour, in particular because of the fact that the law is judge-made.

3 Cf. La Porta, Lopez-De Silanes & Shleifer 2008, p. 286.

4 La Porta *et al.* 1997; La Porta *et al.* 1998; Glaeser & Shleifer 2002; La Porta, Lopez-De Silanes & Shleifer 2008.

5 La Porta *et al.* 1997; cf. La Porta, Lopez-De Silanes & Shleifer 2008, p. 285.

markets, ownership of the media and (mandatory) military service.[6] The core of their claim is that, compared to French civil law and the countries to which this was exported, the common law shows:[7]

> '(a) better investor protection, which in turn is associated with improved financial development, better access to finance, and higher ownership dispersion, (b) lighter government ownership and regulation, which are in turn associated with less corruption, better functioning labor markets, and smaller unofficial economies, and (c) less formalized and more independent judicial systems, which are in turn associated with more secure property rights and better contract enforcement'.

However, many scholars doubt the empirical claim of this literature and criticise its findings both on methodological grounds as on grounds of misconception of differences between the civil law and the common law. This led to a large literature in which not only the legal origins-thesis itself is attacked,[8] but in which the importance of legal origins is also discussed for other fields, such as procedural law,[9] labour law,[10] environmental law[11] and corporate law in general.[12]

Secondly, the question is increasingly asked whether legal institutions and the rule of law are also important in the process whereby poor nations develop their economy. For example Cooter, Schäfer and Ulen[13] have attempted to examine why some developing countries do relatively better than others and found that this is at least partly caused by different legal institutions. However, others point at the fact that legal rules may play some, but perhaps only a modest, role in economic development. A powerful example is in this respect China which, at least at first blush, does not seem to rely strongly on legal institutions (at least in the traditional sense)[14] and nevertheless has experienced a spectacular economic growth.[15] China has continued to have an annual growth rate of its GDP of 9 per cent for most of the past 30 years.[16]Also the recent economic success of civil law countries such as Brazil and Mexico remains puzzling in this debate. This discussion usually takes place under the heading of 'law and development'. Although this field became marginalised in the 1970's, the belief in the power of law reform received renewed impetus in the last decade,[17] possibly also as a result of the influence of the neoliberal Washington Consensus.[18]

6 Cf. La Porta, Lopez-De Silanes & Shleifer 2008, p. 286.
7 La Porta, Lopez-De Silanes & Shleifer 2008, p. 298.
8 Instead of many: Roe 2006 and Siems 2008a, p. 354; a reply to much of the criticism can be found in La Porta, Lopez-De Silanes & Shleifer 2008; also see the special volume of *Brigham Young University Law Review* 2009, p. 1413-1906.
9 Djankov *et al.* 2003.
10 Botero *et al.* 2004.
11 See the references in the contribution of Michael Faure to this volume.
12 See the references in the contribution of Alessio Pacces to this volume.
13 See e.g. Cooter 2006; Cooter & Schäfer 2011.
14 Although in China informal relations, so called 'Guanxi' seem to some extent to replace formal law. See Zhang & Jing 2007.
15 Cf. Ohnesorge 2007.
16 Ulen 2011.
17 See Davies & Trebilcock 2008 and cf. the contribution of Ralf Michaels to this volume.
18 Also see the contribution of Julan Du to this volume.

Thirdly, there is an interesting aspect to this discussion from the viewpoint of comparative law. While comparative lawyers are prone to argue that existing jurisdictions differ from each other in many different ways,[19] they are not particularly good at finding explanations for these differences. While some seek to explain legal diversity from differences in culture[20] and others from varying preferences among citizens,[21] these explanations are not fully satisfactory.[22] The legal origins-thesis claims that differences among the civil law and the common law tradition go back to diverging roles of the administrative and judicial authorities in the very formation of France and England.[23] This has supposedly led to greater judicial independence in common law than in civil law, as well as to a better protection of private property and of enforcement of contracts in common law. The different ways of thinking about the role of the State that came about a long time ago would still prevail as part of separate mentalities in civil law and common law countries, leading to different ways of dealing with State abuse and market failure. They persist because[24]

> 'beliefs and ideologies become incorporated in legal rules, institutions, and education and, as such, are transmitted from one generation to the next. It is this incorporation of beliefs and ideologies into the legal and political infrastructure that enables legal origins to have such persistent consequences for rules, regulations, and economic outcomes'.

The 'toolkit' of civil law would more prominently feature nationalisation and direct State control, whereas common law countries would favour litigation and a belief in the market. When a new problem arises, a civil law country will typically expand the scope of government control while a common law country is more likely to take measures to support the market.[25] However, this claim has not come to play an important role in comparative scholarship.[26] This is pitiful because it could shed new light on understanding differences among jurisdictions.

There is little doubt that these three aspects are all interesting in themselves. Despite their fairly recent publication, the original papers by La Porta, Shleifer and others even belong to the best-cited articles in the field of economics, in which they are broadly debated and criticised.[27] The idea probably found its best-known practical application in the annual Doing Business reports that are published by the

19 Cf. Zweigert & Kötz 1998, p. 63.
20 Legrand 1996, p. 61.
21 Tiebout 1956; Wagner 2005, p. 5. Cf. Levmore 1986.
22 Also see Smits 2011.
23 Cf. Glaeser & Shleifer 2002.
24 La Porta, Lopez-De Silanes & Shleifer 2008, p. 308.
25 La Porta, Lopez-De Silanes & Shleifer 2008, p. 308.
26 The main textbooks remain silent: in the same vein Siems 2008b and Michaels 2009, p. 767. This is even more surprising in view of the fact that comparative lawyers are usually aware of the forceful argument made by Pierre Legrand that civil law and common law show 'unbridgeable' mentalities. Legrand 1996 does not cite La Porta *et al.* and La Porta *et al.* do not cite Legrand, even though both their positions could be made stronger if they did.
27 Cf. Siems 2008.

World Bank since 2003.[28] The idea for these reports was developed under the leadership of Simeon Djankov, based on the article Djankov wrote together with La Porta, Lopez-de Silanes and Shleifer in 2002[29] and which heavily builds upon the legal origins thesis by claiming that countries with heavy regulation on starting a new business are more likely to have higher corruption and a bigger unofficial economy than countries with low regulation. The reports are famous for measuring the costs (in particular in so far as these are caused by regulations and government intervention) of doing business in 183 countries. In many developing countries, the annual reports are seen as an important benchmark and it is often part of the government policy to achieve a higher ranking in the next edition. The very publication of the reports thus promotes law reform from the inside out.

However, it is regrettable that the three mentioned aspects remain largely within their own domains. While the legal origins-thesis is mainly (though not exclusively) discussed by economists (primarily by those working in finance and institutional economics), the debate about law and development also remains mostly separate. In the same vein, the legal origins-thesis is not discussed in mainstream (comparative) law – as La Porta and Shleifer *et al.* in their seminal articles did not take much cognisance of what legal academics wrote about the differences between civil law and common law. It is a safe conclusion to say that the various streams of literature paying attention to the question to what extent legal origins matter for economic growth have not been strongly integrated.[30]

This book aims to overcome this deficiency of the present discussion and attempts to bring the various approaches together. It does so by presenting a wide range of views on how law and economic development are related. The book is loosely divided into three different parts. Part 1 is devoted to general questions and empirics, part 2 to the study of the separate legal traditions and China and part 3 to some specific areas of law. However, it is difficult to separate these three parts entirely: the questions discussed in the various contributions are all highly interrelated.

In the remainder of this Introduction, an attempt is made to summarise the findings of the individual contributions and to place these in the broader context of this book's main question: does law matter for economic growth?

## 2. General Part

The legal origins-thesis and law and development studies are both based on the assumption that law matters for economic development. This implies the existence of some form of causality between a certain set of institutions or legal rules and economic development. The work on legal origins even claims that the present economic development of a country is largely dependent on how the history of that country is shaped. Law and development studies adopt a view of economic growth that is less based on historical accident, but here too it is emphasised that the law

28 The latest edition is World Bank Group 2010; also see <www.doingbusiness.org> (last visited 24 August 2011).

29 Djankov *et al.* 2002.

30 Also see the contribution of Ralf Michaels to this volume.

and the economy are closely linked. However, it is precisely this causal link that is often criticised in the literature. In brief, the main point of criticism is that legal origin is actually a proxy for something else, such as culture, history or politics. In reality, these factors are much more responsible for how a country develops economically than the formal legal institutions. This means that there is a problem of reverse causality: economic growth is not the result of better laws, but better laws come about in countries that have a better functioning economy anyway. It could for example very well be that shareholders are protected better in some countries because of the political pressure that investors can exercise on the lawmaker in these countries.[31]

In the General Part of this volume, several authors deal with this key question and with other points of methodology. The first is Ralf Michaels who, in an insightful contribution, discusses the interconnectedness of the legal origins-claim and functionalism as used in comparative law. Michaels clearly shows that the legal origins-thesis is largely dependent on the functionalist method. Glaeser and Shleifer[32] for example heavily rely on functionalism when they identify as a common problem of all legal systems the need to protect law enforcers against physical force and bribes. The French solution of centralising the law is in their view thus functionally equivalent to the English solution of creating a jury-based legal system. The main point made by Michaels is that many of the objections that can be brought in against such (and other types of) functionalism can also be held against the legal origins-literature. It is surprising that while these critiques of functionalism have been lethal elsewhere (and in particular for the law and development-movement), they have not led to the demise of the legal origins-thesis. Michaels explains this 'strange lure of economics' by its ability to show results in the form of statistics and objective-looking data and rankings. The theoretical and empirical foundations of the legal origins-literature should therefore be revisited and thought through in a better way. One challenge presented by Michaels is the possibility to integrate the functionalist approach with culturalist comparative law. One way of doing this may be a combination of statistical analysis and case studies.

The point made by Ralf Michaels is taken up in the contribution by John Armour, Simon Deakin, Viviana Mollica and Mathias Siems.[33] One way in which the existing work on legal origins can be ameliorated is by making use of alternative empirical testing. A major point of criticism is that the data used by La Porta *et al.* are largely based on cross-sectional datasets, only providing evidence on the state of the law at limited points in time. Armour *et al.* show what we can learn from so-called time-series evidence, which considers legal variations over time. Their contribution is important in criticising one of the central points of the legal origins-literature: they show that, in a time-series analysis, an increase of shareholder rights does not foster economic development. More in general, they also cast doubt on the explanatory force of legal origins as an external factor explaining economic

31 La Porta, Lopez-De Silanes & Shleifer 2008, p. 298 & 310.

32 Glaeser & Shleifer 2002.

33 Previously published in *Brigham Young University Law Review* 2009, 1435-1500 and reprinted in this volume with the kind permission of the authors and the publisher. Also see Armour *et al.* 2009.

development and find it more plausible – in line with the general criticism on legal origins – that the legal system evolves in parallel with changes in national economic conditions and political structures.

An even more sceptical perspective is provided by Eric Helland and Jonathan Klick. In their contribution, they severely doubt the empirical credibility of the legal origins-thesis as such. The fundamental problem they see is one of statistical identification: although there is little doubt that there are correlations between various legal institutions and economic outcomes, one cannot claim with any certainty that these correlations provide evidence of causality. Helland and Klick convincingly show that the work of La Porta *et al.* is not robust, leading them to conclude that 'despite its tremendous influence in both academic and policy circles, the empirical estimates from the legal origins literature are simply not credible'. What is more, the authors also doubt whether present micro-economic tools can be used at all to establish a causal relationship between economic growth and legal institutions.[34] To draw policy conclusions about which legal rules should be adopted to promote economic growth is in any event premature.

This conclusion calls for a turning back to the very foundations of what it means 'to turn law into numbers'. Mathias Siems discusses this fundamental question. He makes clear that when economists measure legal rules and institutions, their approach is often a 'just do it' one, implicitly assuming that the complexity of the law does not prevent it from being turned into numbers. This is exactly the point that Ralf Michaels complained when he spoke about the 'strange lure of economics'. Legal academics, by contrast, typically have the attitude of 'just don't do it', often claiming that the law is not quantifiable. Siems explains and discusses six different ways of how law can be measured. For all methods, the measurement of law is not straightforward. This calls for more collaboration across disciplines and in particular for economists and other social scientists to benefit from lawyers' more sceptical attitude towards quantification.

This call for more collaboration and an interdisciplinary approach to the analysis of institutional change is shared by Giuseppe Dari-Mattiacci and Carmine Guerriero. In their contribution, they offer an account of how to understand the origins of formal and informal institutions of regulation and their impact on present day law. Their approach is also sceptical: it is impossible to establish causality between legal origins and a certain level of economic development. However, the important point made by them is that the civil law-common law-distinction is too simple to understand comparative variation: modern societies witness a wide variety of sources of law next to courts and legislatures. The analysis should therefore be broadened to include inter alia the internal functioning of lawmaking institutions and the complex interaction among different sources of law.

Robert D. Cooter and Hans-Bernd Schäfer discuss another point of methodology: what does economic growth exactly mean? While they recognise that law greatly matters for economic development, it is not so clear what criterion should be used to measure it. Cooter and Schäfer distinguish between wealth making and wealth taking and make a clear case for how influential the law can be in striking the balance between the makers and takers of wealth. They show with abundant

[34] Also see Klick 2010.

examples how wealth can be taken from others in a criminal way (through theft and bribes), in a political way (through subsidies and regulations) and by the workings of the market (through cartels and monopolies) and how wealth can be made through the work of entrepreneurs, labourers, farmers, shopkeepers etc. The traditional Marxian labour theory of value and the micro-economic marginal productivity theory are not satisfactory in measuring how much wealth is created by this and they should be replaced by a novel theory on productivity of entrepreneurs who supply economic innovations.

Cooter and Schäfer thus share the basic insight of the legal origins-scholarship on the importance of law. However, the important point they make is that it depends entirely on one's definition of wealth (hence on the exact balance between taking and making of wealth) when exactly the law will promote economic welfare and when it will not. If people get their wealth by taking it from others, economic growth will be fostered by the abolition of capital markets. However, if wealth comes mostly from fostering innovation – as seems to be the case today as the world's richest people all collected their richness by some form of innovation – the law should primarily protect investors and secure (intellectual) property rights. Law can cause growth, but it depends on the source of growth which institutions and rules are best suited to guarantee this growth.

The question of how exactly different legal systems matter for economic development is also taken up in the contribution of Anthony Ogus on legal systems as networks. He shows how characteristics of networks apply to features within a legal system and to legal systems as a whole. This line of thinking emphasises that the value to a single user of a product or a service depends on the number of other users, meaning that the social value of the network increases if more users adopt it. The great value of Ogus' contribution lies in the fact that he links the discussion about legal origins to the value of competition among legal networks. As Ogus states:

> 'A – perhaps the – key variable in evaluating the impact of legal systems on economic growth in developing countries is how well a legal network originally externally imposed by colonialist regimes is adaptable to local conditions and pre-existing local legal networks'.

A dominant legal network – such as that of the former colonialist power – will only evolve efficiently if it is subject to competition, thwarting the ability of practitioners to capture rents by manipulating the law. Interestingly, this aspect does not feature in the work of La Porta et al. although it seems vital to understanding how successful a legal system is. It is in this respect also useful to refer to the work of Stefan Voigt who, in an article published in 2008,35 expressed doubts about the superiority of the common law in view of the possibility of choice of law: if the legal origins-thesis is right, it would mean that rational actors would choose a common law jurisdiction as the applicable law – for which there is no conclusive evidence.

The final chapter in this part by Thomas Ulen argues powerfully that law may not be a necessary, but not even a sufficient condition for economic growth. One

35 Voigt 2008.

reason for a sceptical attitude towards the importance of law is that there may be important alternatives to law, such as social norms, which can largely fulfil the same role. To some extent social norms can hence fulfil the same societal functions as a well functioning modern legal system.[36] In addition the case of China, so Ulen argues, powerfully shows that even in the absence of formal legal institutions economic growth is still possible. China sustained a spectacular economic growth even though formal legal institutions were largely lacking. Ulen in addition argues that the case of China also demonstrates that democracy is not a precondition for economic growth.[37] In fact stability may be a crucial factor in promoting economic growth which may be easier to guarantee in more centrally controlled (not necessarily democratic) forms of government. Finally Ulen also points at the important role of political leaders and more particularly their political courage to engage in changes which can provide the necessary environment to foster economic growth.

In sum, the contributions to this first general part all take to some extent the legal origins literature as a starting point, but at the same time provide important nuances and criticisms. It is striking that criticisms, although of a different nature, are formulated both from an economic as well as from a legal perspective. From a legal perspective criticism is, for example, formulated on the 'strange lure of economics' to turn results in the form of statistics and objective looking data and rankings, thereby ignoring the fundamental question whether it is possible at all to 'turn law into numbers' (see Michaels and Siems). Criticism is equally formulated on the rather unbalanced way in which distinctions between the civil law and common law are presented, thereby largely ignoring the differences between the particular legal systems (see Dari Mattiacci and Guerriero).

More fundamentally the question is also asked whether it is at all possible to show a causal relationship between particular legal institutions and economic growth. If, in a time–series analysis the results of the legal origins literature are addressed in a more detailed manner the results are not sustained. This is, for example, what Armour *et al*. show with respect to the relationship between an increase of shareholder rights and economic growth. Helland and Klick also show that when the methodology of the legal origins literature is critically analysed the results are simply not robust. This leads them to doubt whether it is at all possible to prove a causal relationship between particular legal rules and economic growth.

Already these insights are important since at the policy level too easily normative conclusions were drawn from the legal origins literature e.g. on the importance of developing legal institutions in developing countries, but also on a preference for the common law. The chapters in this part show that to an important extent these policy advises may have been misguided also because (as Ulen powerfully argues) many other aspects than simply legal rules can be important in promoting economic growth.

Moreover, the chapters in this part are on the one hand doubting whether it is at all possible to show causal relationships between legal rules and economic growth, but on the other hand also provide indications for different approaches to the question how the quality of legal rules and the importance of legal institutions

36 This builds on the insights of Ellickson 1986, and Ellickson 1991.
37 Following the work of Lipset 1959.

can be measured. Michaels and Siems both argue in favour of combining statistics with a more qualitative approach, using also the virtues of comparative law and, for example, combining statistics with a case studies approach. These approaches may provide more nuanced and therefore more valuable insights than a mere statistical approach, which seems to provide objective results, but which are not robust either and therefore even misleading.

## 3. Common Law, Civil Law and China

After the general and methodological insights provided in the first part, the second part of this volume considers the common law, civil law and China. For the purpose of this book, it is in particular important to look in detail at the suggested superiority of the common law compared to other jurisdictions. France (discussed by Bernard Crettez, Bruno Deffains, Guillaume Leyte and Laurent Pfister) and China are in this respect highly useful countries to consider. This does not need much explanation for France as this is the typical civil law country and also the jurisdiction that La Porta *et al.* consider as the main exporter of civil law. China is evidently interesting because of its spectacular economic development despite the absence of formal legal institutions as we know in the Western world.

Nuno Garoupa and Carlos Gómez go to the core of the legal origins-claim by reviewing the argument that the common law provides better incentives to induce efficient behaviour. They review the reasons why the common law may be more efficient, but conclude that these reasons are not satisfactory. And even if the common law would be evolving towards efficiency, this cannot explain persisting differences among common law jurisdictions: in each country where the common law found root, local circumstances made it depart from original English law. A more realistic account of the efficiency hypothesis of the common law is therefore that there is not one single efficient rule, but that different adequate rules exist dependent on the local circumstances. Their main conclusion is therefore that there

is no conclusive evidence that French civil law is inferior because of a lack of efficiency. This conclusion is reinforced by the experience of mixed jurisdictions: if the stance of the legal origins-claim is that mixed legal families should give up the civil law aspect of their jurisdiction in search of efficiency, this is very unlikely to promote economic growth – if it were only because this would violate the prevailing local institutional arrangements in those jurisdictions.

The point that legal institutions (and the way in which they came about) do not have an overriding influence on economic development is also taken up by Bernard Crettez, Bruno Deffains, Guillaume Leyte and Laurent Pfister. In their contribution on the law and economics of the French Civil Code, they make clear that a legal system is not independent of the values of society and that therefore there is no reason why there would be one unique legal system (such as the common law) to favour economic growth. Their article builds upon the work by Arranuda and Andanova,[38] who have attempted to explain the formation of the French Civil Code from the behaviour of judges. Before the French Revolution, French judges were hostile to the market system: the courts were mostly populated with the nobility without much knowledge of (or sympathy for) merchants and their interests. In post-Revolutionary France, the only way to inhibit judges with a more market-friendly approach was to restrict their powers. This was done by making judges civil servants and by drafting a Code that took better account of commercial parties. This Commercial Code had, alongside the new Civil Code, to be interpreted strictly. In brief: the only way in which economic growth could be enhanced was by intervention of the legislature, forcing judges to make more market-oriented decisions. Also in the work of Lagarde,[39] the two Codes are presented as means to assure a desired order: next to the social order created by the Civil Code, the Commercial Code would foster risk-taking relationships. Despite the criticism of Crettez, Deffains, Leyte and Pfister on the views of both Arranuda and Andanova and Lagarde, they do acknowledge that they offer insightful explanations of why the French Civil Code came about. However, we should also submit that the historical account of Arranuda and Andanova is not too far apart from the legal origins-claim that French law is typically used as an instrument in the hands of the State. The question that remains unanswered is how this would affect the economic development compared to countries where the State plays a less important role.

Under the provocative title 'Does China need law for economic development?', Julan Du discusses the spectacular rise of China that does not seem to fit any of the predictions of the legal origins-literature. Despite the absence of formal legal institutions and a conception of the rule of law after the Western model, China has experienced an annual average growth rate of 9,5 per cent since 1978. China is now the second largest economy in the world, but ranks 79 in the 2011 World Business Report ranking on the ease of doing business.[40] Du asks how to explain this puzzle of the coupling of economic success and weak legal institutions and provides a fascinating explanation. He argues that the Chinese government acts as a substitute

38 Arranuda & Andonova 2005, and Arranuda & Andonova 2008.
39 E.g. Lagarde 2009.
40 World Bank Group 2010, p. 4.

for formal legal institutions in guaranteeing a stable business environment: in China, laws do not have the function of protecting entrepreneurs against governments and bureaucracy, but are instruments of the State to implement its policies. Du shows convincingly that this role of the State is pervasive and also extends to the role that courts traditionally have in Western countries. The examples he gives from commercial dispute resolution, corporate governance and regulation of financial markets show how authorities can take over the functions of courts and of the rule of law in helping entrepreneurs. Although this 'helping-hand regulatory State model' is now under pressure, its important role in the past does explain why China could develop its economy in the way it did. The important lesson for the legal origins-debate is clear: even though the judiciary in China is very weak in Western eyes, China does have a stabile economic growth thanks to the helping-hand regulatory state model that has largely filled the void left by the absence of formal legal institutions.

In sum, the chapters in this part to a large extent confirm the points made in the general part, by looking in a more detailed way at civil law, common law and the particular case of China. Like Dari Mattiacci and Guerriero already held in the previous part, Garoupa and Gómez also come to the conclusion that there is no inherent reason neither theoretically nor empirically to hold that the common law would be superior to the civil law in promoting economic growth. The findings of Du on China also confirm what was mentioned in the previous part by Ulen, being that China is apparently able to sustain economic growth without western style legal rules or a western style democracy. This puts the importance of legal rules in promoting economic growth into perspective since it shows that there may be alternatives to traditional legal rules which could replace its role. In the case of China it may be a strong central government, combined with social norms. This has, as Ulen also argued in the previous part, important normative implications. International institutions such as the World Bank strongly believe both in the importance of legal institutions to promote economic growth and in the superiority of the common law. This often led to policy advises to developing countries holding that the development of legal institutions would guarantee economic growth. Ulen argues in his chapter that this advice often seemed misguided as the expected economic growth did not follow. The chapters in this part show that this should to some extent not come as a surprise on the one hand since the legal transplants imposed upon developing countries may not always fit the receiving legal system (for example when common law rules would be imposed in a civil law jurisdiction) and the case of China underscores the fact developing countries may have alternatives which can fulfil the same role as legal rules in promoting economic growth.

## 4. Specific Fields of Law

The third and final part of this volume provides insights from some specific fields of law. As already mentioned in section 1, the debate about law and economic growth is not limited to corporate governance but was also taken up for other fields. In this part corporate law, property law and environmental law are discussed.

Corporate law is the field on which the first papers by La Porta *et al.* were written and it remains one of the most interesting fields to analyse to what extent law matters for economic growth, also because of the clearly distinctive models of

corporate governance that have been adopted throughout the world. In his contribution, Alessio Pacces critically reviews the 'law and finance' literature that seeks to identify efficient corporate law by identifying the shareholders as the actors best suited to maximise the value of the firm. Pacces does not see convincing empirical arguments for the superiority of dispersed ownership. In his view, corporate law should be neutral to the ownership structure and enable both controlling shareholders and managers to be in control, as long as they are committed not to expropriate investors. On a more general note, Pacces notes what we saw before in part 1 of this volume: the problem with the 'law matters'-argument is that it is methodologically difficult to make. Legal protection of shareholders may not be the only institutional factor affecting the choice of corporate governance arrangements, let alone economic development. This makes the ambition of the law and finance scholarship to identify the 'best' system of corporate governance a failed one.

Guangdong Xu asks about the relationship between property rights and economic performance. It is common knowledge that effective property rights are vital to economic development: they create incentives for individuals to carry out productive activities such as investment, trade, and creation of wealth. In the context of this volume, however, the interesting question is whether one specific type of designing property rights is better for economic development than another. Xu's discussion of the available empirical evidence shows that this provides us with a puzzle: despite the advantages of formal ownership claimed by economists and lawyers, formal property rights and land titling fail in most developing countries. This is not surprising as mere formalisation is not enough: good governance (including a consistent legal and institutional framework, access to information, and impartial agencies) is necessary for the functioning of formal property rights. In line with the lessons from China taught by Julan Du, Xu makes clear that the question how property rights matter is a complex one: its answer depends on how the local market in question works and how it interacts with the economy, polity, and society in general. Again, it is submitted that it is naïve to embrace property privatisation and formalisation as a means to create economic growth as this may work in some countries, but not in others.

Michael Faure has addressed the relationship between environmental law and economic growth from two separate angles. There is on the one hand an impressive literature addressing the question whether economic growth will lead to an increased environmental pollution. This literature is known as the Environmental Kuznets Curve which roughly shows that increasing income per capita first leads to increasing pollution levels, but later after reaching a turning point to decreasing pollution levels. Even though there has been substantial criticism on this EKC literature some empirical studies show that environmental quality did indeed increase with economic growth, but only when this was supported by decent environmental regulations, in other words institution. Again, the World Bank had originally supported economic growth arguing that this will automatically lead to

better environmental quality, also for developing countries. Recent studies show that this is only the case when countries also enact effective environmental policies. There is hence no automatism in the relationship between per capita income and environmental quality; the quality of environmental law also matters. Another aspect is whether countries engage in a competition to attract industry with lenient environmental regulation, seducing industry to relocate to so-called pollution havens. The theoretical conditions for such a pollution haven hypothesis are highly debated. Some indeed argue that states will engage in a race to the bottom to attract industry with lax environmental regulations. Others argue that under different assumptions states could also benefit from strict environmental regulations (improving their competitive position trough technological innovations), hence leading to a race to the top. Empirical evidence for both hypothesis exists. Empirical evidence does confirm that even though industry may not necessarily relocate to pollution havens, pollution control costs do matter in the *ex ante* decision of industry on choosing an appropriate location.

In sum, the contributions in this part, addressing the relationship between particular fields of law and economic growth also come to nuanced conclusions in the sense that this relationship very much depends on particular circumstances. As far as corporate law is concerned Pacces showed that shareholder protection may not be the only institutional factor affecting the choice of corporate governance arrangements and Xu comes to a similar conclusion as far as property rights are concerned: the institution of property rights alone does not guarantee economic growth, since this depends on a number of other factors related to good governance. A similar nuanced conclusion was reached with respect to the relationship between economic growth and environmental policy: economic growth may lead to increased environmental quality, but again this may depend on the type of pollutants involved and also the institutional circumstances. The chapters show, in other words, that the truth is again in the detail and that the particular relationship between the fields of law and economic growth very much depends upon particular circumstances.

## 5. Conclusions

We argued above that there were several reasons to produce a multi-disciplinary volume addressing the relationship between legal rules and economic growth from both a legal and an economic perspective. One reason was the apparent contradiction between on the one hand the large attention attached to the legal origins literature by economists and on the other hand the large criticism that is equally formulated on this literature both by economists and by lawyers. The contributions to this book have hopefully contributed to a better understanding of the strengths, but also the methodological weaknesses of the legal origins literature by showing both the problematic nature of attempts to quantify the quality of legal rules, but also the empirical weaknesses and limited robustness of the legal origins literature.

Another reason to pay attention to this topic is that it has strongly influenced the question of what poor countries should do to become rich. The legal origins

literature roughly advised not only that legal institutions would generally be important to guarantee economic growth, but that, moreover, institutions originating from the common law may be superior in reaching that goal. These recommendations have been taken seriously at the policy level and have led e.g. via the so called 'Washington consensus' to recommendations to developing countries to focus primarily on the development of stable legal institutions. However, many agree that a few decennia later the results of this policy seem to have been relatively poor. On the one hand not all countries that introduced legal institutions had economic growth and on the other hand some countries (more particularly China) experienced a strong economic growth, even in the absence of legal institutions. Several contributors to this book try to explain this phenomenon, largely arguing that legal institutions may not always be a necessary condition for economic growth (to the extent that other rules or institutions (such as social norms or a strong government) can be adequate substitutes for legal rules); in addition legal rules may not be a sufficient condition for economic growth either since other parameters related to the broad notion of good governance may also be needed to reach a sustained economic growth.

A final reason for this book was that there was apparent mismatch between on the one hand the large debate on the 'law matters' literature in economic and on the other hand comparative law. To a large extent the nuances and differences pointed at in comparative legal scholarship were largely ignored in the legal origins literature. Hence, it remains an open question why legal systems largely differ from each other and whether this can be explained by economics alone. One goal of this book was to somehow bridge this gap and move towards an integration of the economic (statistical) approach and the legal (more qualitative case based) approach.

The contributions to this book have contributed to this important debate on the relationship between legal rules and economic growth, but the issue is of course so demanding and complicated that much more research will be needed. Several contributors to this book have, precisely in an attempt to bridge the legal and the economic approach, provided suggestions on how the statistical approach followed by economists could be supplemented with a more qualitative approach followed by lawyers, e.g. via the use of case studies. Also the chapters looking at the relationship between particular legal rules (in the fields of environmental, corporate and property law) and economic growth show that it is difficult to reach general conclusions and that this relationship may depend upon a number of specific details and circumstances. The key is of course to distinguish these particular circumstances as they may provide more useful insights on how particular legal institutions may, depending upon the circumstances, contribute to economic growth or not.

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