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What is Law & Development?

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Law & Development studies have been growing in the past few years, after having its death declared in the 1970s.[1] There is, however, very little clarity as to what this field of study encompasses or whether it is a field at all.[2] Under the label of Law & Development one can find a wide variety of studies, approaches, analyses and topics. Some studies focus on formal institutions, discussing how enforcement of contracts, protection of property rights, and an independent judiciary protect investors and improve economic growth in developing countries.[3] Others have not focused on economic development, but instead on how laws to protect women from abuses in the family and to create quotas to guarantee their participation in the public sphere have been largely ineffective due to deeply embedded social norms and values that cannot be changed by legislation (at least

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[1] David M. Trubek & Marc Galanter, "Scholars in Self-Estrangement: Some Reflections on the Crisis in Law and Development." (1974) Wisconsin Law Review 1062.

[2] Brian Z. Tamanaha, 'The Primacy of Society and the Failure of Law and Development', *Cornell International Law Journal* (forthcoming) [Tamanaha, "Primacy of Society].

[3] See for example Robert Cooter and Hans-Bernd Schaefer, *Law and the Poverty of Nations* (forthcoming), p. 12; see also Kenneth Dam, *The Law-Growth Nexus: The Rule of Law and Economic Development* (Washington: The Brookings Institute Press, 2006) at 91.

not from one day to the next).[4] Still others have criticized the Law & Development discourse as another source of imperialism and dominance that justify senseless legal transplants from the North to the South.[5]

What brings all these studies together under one label? What is it that one should know, if one is looking for a concise summary of what this field of study encompasses? These are the questions that I will try to answer in this essay. The reader should be forewarned that the title may be slightly misleading, as the paper will not provide comprehensive and conclusive answers to the question "What is Law & Development?" but hopefully it will offer a starting point for a deeper inquiry. Most importantly, I hope readers will take this as an invitation to explore this field in greater depth.

1. The relationship(s) between Law and Development

More than 1 billion people in the world today live on less than a dollar a day,[6] and since World War II a number of scholars have taken up the challenge of understanding this phenomenon. Why are some countries rich and others poor? Why are there certain regions or communities around the world that have persistently low income, lower levels of education and poor health indicators? Why have these communities not been able to thrive as much as others? These are some of the questions that development scholars try to answer. In addition to attempting to identify the causes of this phenomenon, many development theories have influenced or inspired concrete policy proposals that try to tackle the problem of development around the world.[7]

What is the relationship between law and development? How is law related to problems such as low income, lack of education and poor health? Different Law & Development scholars provide different answers to these questions. This is one of the reasons why it is hard to present a definition of the "field" of Law & Development, let alone argue that this is a field of study that embodies a precise, unified and cohesive set of assumptions and concepts.

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[4] See for example Monica Das Gupta, "State Policies and Women's Autonomy in China, The Republic of Korea, and India 1950-2000: Lessons from Contrasting Experiences", in Vijayendra Rao & Michael Walton, *Culture and Public Action* (Satanford: Stanford University Press; 2004).

[5] Trubek & Galanter, *supra* note 1. But see Brian Z. Tamanaha, "The Lessons of Law-and-Development Studies", American Journal of International Law 89 (1995), pp. 470-486.

[6] United Nations, *Millennium Development Goals Report 2010*, available at http://www.un.org/millenniumgoals/pdf/MDG%20Report%202010%20En%20r15%20-low%20res%2020100615%20-.pdf

[7] For an intellectual history of the concept of development, see Heinz W. Arndt, *Economic Development: The History of an Idea* (Chicago: The University of Chicago Press, 1987).

Despite this lack of cohesiveness in the field, it is possible to aggregate the works of different Law & Development scholars into two main groups. One group analyzes how law can play an instrumental role in achieving development goals. This is what could be called *law in development.* The other group views legal reforms and the rule of law as an end in themselves. This is what I would call *law as development.*[8]

1.1 Law in Development

Law can serve as an instrument to promote development. This pragmatic and instrumental view of the law and the legal system is shared by scholars who think that legal reforms can be a means to advance certain development goals, such as economic development as measured by a country's GDP per capita. However, these scholars do not always agree on *how* law can promote development. These divergences are largely based on different views of the role of the state in promoting development in general and economic growth in particular.

One school of thought advocates a strong role for the state in promoting development. The concept of developmental state was coined to describe countries in which there was (or there is) strong state intervention in the economy, significant protections for national industries, and heavy regulation of multinational corporations that decide to invest in subsidiaries in these countries. Some examples of successful developmental states are Japan, Singapore and South Korea.[9] Not so successful examples include Brazil and India in the 1970s and 1980s.[10] In the developmental state, law can be used as an instrument for state intervention in economic activities. This intervention may in turn lead to economic growth.

> Law is needed to create the formal structure for macroeconomic control. Legislation can translate policy goals into action by channeling economic behavior in accordance with national plans. The law is needed to create the framework for operation of an efficient governmental bureaucracy and

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[8] This typology is inspired by the historical overview of the three moments of the law and development movement elaborated by David Trubek & Alvaro Santos (eds.). *The New Law and Economic Development: A Critical Appraisal* (Cambridge: Cambridge University Press, 2006) [Trubek & Santos, *New Law and Economic Development*]. For a more comprehensive overview, see Kevin E. Davis and Michael J. Trebilcock, "The Relationship between Law and Development: Optimists versus Skeptics", (2008) American Journal of Comparative Law, Vol. 56, No. 4.

[9] See Chalmers Johnson, *MITI and the Japanese Miracle* (Stanford: Stanford University Press, 1982) and Meredith Woo-Cumings (ed.), *The Developmental State (*Ithaca, NY: Cornell University Press, 1999).

[10] Peter Evans, *Embedded Autonomy: States and Industrial Transformation (*Princeton: Princeton University Press, 1995).

> the governance of public sector corporations. Legal rules are needed to manage complex exchange controls and import regulations.[11]

This school of thought could be called *law in the developmental state.*

Another school of thought subscribes to neoliberal theories of development, which advocate minimal state intervention in the economy.[12] Markets are considered the engine for growth for these scholars. Thus, state intervention in economic activity is discouraged, and the state's role is limited to providing the conditions for private actors to act freely. Thus, the state should simply secure the legal and institutional basis for free market activities to take place. In this context, Law & Development focuses on "private law in order to protect property and facilitate contractual exchange. It [seeks] to use law to place strict limits on state intervention and ensure equal treatment for foreign capital."[13] This second school of thought could be labeled *law in the neoliberal state.*

Despite the divergent views of the role of the state, these two schools of thought share the assumption that law can play an instrumental role in promoting development, and especially economic growth. Historically, the second view (law in the neoliberal state) has succeeded the first view (law in the developmental state), which was in turn succeeded by the third view presented below,[14] which is currently highly influential in most of the Law & Development scholarship.

1.2 Law as Development

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[11] Trubek & Santos, *New Law and Economic Development, supra* note 8 at 5.

[12] In the 1980s, the neoliberal theory was embodied in a set of policy prescriptions that became known as the "Washington Consensus". The central tenets of the Consensus were: macro-economic stability (fiscal discipline, tax reforms and reduction in public expenditures), liberalization (open trade and market deregulation), privatization, and policies to attract foreign direct investment (FDI) and stimulate private entrepreneurship (reduction of tax burdens, availability of credit for private investors, and fostering of competition within sectors). John Williamson, "The Washington consensus as policy prescription for development," in Timothy Besley and Roberto Zagha (eds.) *Development Challenges in the 1990s: Leading policymakers speak from experience*, (New York: World Bank/Oxford University Press, 2005) at 33-61. The Washington Consensus was closely followed by Latin American countries, and more cautiously by developing countries in other regions. V. Bulmer-Thomas, *The Economic History of Latin America since Indepedence* Vol. 2 (Cambridge: Cambridge University Press, 2003). For criticisms, see Moises Naim, "Washington Consensus or Washington Confusion?" (2000) Foreign Policy at 87-103 and Dani Rodrik, "Growth strategies," in Philippe Aghion and Steven Durlauf (eds.), *Handbook of Economic Growth*, (Cambridge: Elsevier, 2005). Chapter available at: www.ksg.harvard.edu/rodrik/.

[13] Trubek & Santos, *New Law and Economic Development, supra* note 8, pp. 5-6.

[14] Ibid., pp. 6-7.

In contrast to the instrumental view described above, some scholars conceive legal reforms and the rule of law as an ends in themselves.

> From a deontological perspective, such as that adopted by Sen, where freedom, in its various dimensions, is both the end and means of development, various freedoms, such as freedom from torture and other abuses of civil liberties by tyrannical rulers, freedom of expression, freedom of political association, freedom of political opposition and dissent, are defining normative characteristics of development; rule of law, to the extent that it guarantees these freedoms, has an intrinsic value, independent of its effect on various other measures of development and does not need to be justified solely in instrumental terms.[15]

While the two groups described above (law in the developmental and the neoliberal state) are largely focused on economic growth, measured by the GDP per capita, law as development is intrinsically connected with the concept of development as freedom, proposed by Nobel laureate Amartya Sen. Sen's concept of development as freedom has moved away from a focus on economic growth, which had been the form of development studies for much of the post-WWII period. Sen states

> we generally have excellent reasons for wanting more income or wealth. This is not because income and wealth are desirable for their own sake, but because, typically, they are admirable general purpose means for having more freedom to lead the kind of lives we have a reason to value.[16]

Based on this idea that wealth is not an end in itself but a means to realize more choices and therefore more freedom, Sen elaborates on the distinction between the ends and the means of development.[17] Thus, economic growth is important because it allows us to live the lives we have a reason to value, which is the end of development. But wealth alone does not guarantee that we will be free. Indeed, there is a series of instrumental freedoms that directly or indirectly allow people to choose to live as they would like. According to Sen, development as freedom requires political freedoms,

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[15] For a detailed discussion about the different conceptions of the rule of law (differentiating thin and thick conceptions), see Michael J. Trebilcock and Ronald J. Daniels, *Rule of Law Reform and Development: Charting the Fragile Path of Progress* (Edward Elgar, 2008) at 4-5. See also Alvaro Santos, "The World Bank's Uses of the 'Rule of Law' Promise in Economic Development", in Trubek & Santos, *New Law and Economic Development, supra* note at 256-266.

[16] Amartya Sen, *Development as Freedom* (New York: Anchor Books, 1999) p. 14.

[17] Ibid. at chapter 2.

economic facilities, social opportunities, transparency guarantees, and protective security.[18]

This concept of development has inspired the United Nations Development Program (UNDP) in an annual series of Human Development Reports dating back to 1990 to conceive a Human Development Index (HDI).[19] The index is based on three ends of development: longevity as measured by life expectancy at birth; knowledge as measured by weighted average of adult literacy and mean years of schooling; and standard of living as measured by real per capita income.[20] While there is a strong positive correlation between income per capita, health and education status, this correlation is not perfect, and indeed rankings of developing countries often change significantly, either upwards or downwards. This means that the ranking of a country may change when health and education variables are incorporated in the Index, along with a per capita income variable. For instance, Vietnam, Chile and Cuba fare better on the human development ranking than on an income ranking, whereas Bahrain, Angola and the United States do worse on the HDI ranking than on the GNP per capita ranking.[21] In sum, the index has shown that there is not necessarily a strong correlation between wealth and these other development goals.

In addition to moving away from an exclusive focus on economic growth, another important claim in the work of Amartya Sen is that the instrumental freedoms are interconnected. For instance, with greater wealth one may be able to achieve better levels of education and have better health.[22] Similarly, one's performance at school or on the job depends on one's health. Thus, there should not be a priority list among these goals, but instead they should be promoted simultaneously. By identifying this interconnectedness, Sen suggests that in many aspects *law in development* and *law as development* are not as far apart as one might assume at first glance. A commitment to protecting the freedoms guaranteed by the rule of law as ends in themselves can concomitantly serve an instrumental purpose in achieving other development goals.[23]

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[18] Ibid. at 38.

[19] United Nations Development Programme, "Origins of the Human Development Approach," *Human Development Reports* (Retrieved May 15, 2009) http://hdr.undp.org/en/humandev/origins/

[20] Ibid.

[21] Ibid. These discrepancies have persisted since 1990. See UNDP, "Defining and Measuring Human Development", *Human Development Report* (1990), p. 14-16.

[22] Ibid., p. 40-41.

[23] Sen, A. "What is the Role of Legal and Judicial Reforms in the Development Process", Speech to the World Bank Conference, June 5 2000.

2. The methodologies of Law & Development

What kind of methodology do Law & Development scholars use to tackle the problem of development? Again, it depends on the scholar. There is no homogeneous methodology in this field, but a plurality of methodologies and approaches. This may be related to the fact that the field of development studies in itself is already an interdisciplinary field. Development economics has certainly been at the centre stage in development studies, but it has not been alone. Other social sciences -- such as political sciences, sociology and anthropology -- have also taken part in the development field and influenced some of its twists and turns.[24] As a result, there is not one field that has influenced Law & Development and therefore the multiple methodologies used in each of these fields can often be found in the Law & Development scholarship.

These methodological differences can easily turn into substantive disagreements about the field. For example, Law & Development scholars may diverge as to how effective law can be in changing undesirable behaviour and therefore in promoting development. Some scholars follow more closely the assumption that individuals are rational actors who respond to incentives. In this sense, very much along the lines outlined by Law & Economics scholars, they suggest that we can incentivize more productive behaviour by reducing costs and increasing outputs.[25] As Ulen and Cooter explain in the Law & Economics context:

> Economics provide a scientific theory to predict the effects of legal sanctions on behavior. To economists, sanctions look like prices, and presumably, people respond to these sanctions much as they respond to prices. People respond to higher prices by consuming less of the more expensive good, so presumably people respond to heavier legal sanctions by doing less of the sanctioned activity. Economics has mathematically precise theories (price theory and game theory) and empirically sound methods (statistics and econometrics) of analyzing the effects of prices on behavior.[26]

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[24] For an analysis of how anthropology has contributed to the field, see R. D. Grillo, "Antropologists and Development", in Vandana Desai and Robert Potter (eds.), *The Companion to Development Studies* (great Britain: Hodder Arnold, 2002).

[25] Douglass C. North, *Institutions, Institutional Change and Economic Performance* (Cambridge: Cambridge University Press, 1990). Julio Faundez, *Good Governance and Law: Legal and Institutional Reform in Developing Countries* (New York: St. Martin's Press, 1997).

[26] Thomas Ulen and Robert Cooter, *Law and Economics*, 3rd ed. (Addision Wesley, 2000) p. 3. For an example of the application of these ideas in the Law & Development context, see Robert Cooter and Hans Bernd Schaefer, "Academic Scribblers and Defunct Economists", *University of Toronto Law Journal* Volume 60, Issue 2 (2010), pp. 467- 489.

The assumption here is that law has the potential to change individual behaviour. If increased costs will make people refrain from acting, reduced costs will incentivize them to act in a certain way. In the Law & Development context this has been translated, for instance, into policy prescriptions for developing countries to attract foreign direct investment (FDI). Legal reform and modernization in both law creation and implementation has been advocated as beneficial for attracting FDI.[27] These prescriptions assume that it is of central importance to foreign investors that the host government does not violate, or inadequately protect, their property rights. Another central component of a legal system conducive to FDI is one that ensures low levels of corruption and also has effective and predictable levels of law enforcement. Laws can promote efficiency through effective resolution of conflicts and regulation that makes doing business easier. This is the assumption of the Doing Business Reports, a World Bank project that aims to investigate "the scope and manner of regulations that enhance business activity and those that constrain it."[28]

In contrast, there are studies that look at individual behaviour from a sociological perspective. These Doing Business Reports, for instance, have been roundly criticized for misrepresenting and oversimplifying information by empirically presenting legal issues that are inherently complex and difficult to measure.[29] One of the criticisms is that by looking only at regulation and law the reports miss the normative or cultural determinants of business activity. Amanda Perry, for instance, claims that there is little empirical evidence that firms are attracted to legal systems that meet the above description.[30] This is supported by the example of FDI in China, which is very high despite an unpredictable legal system.[31] Perry claims that this is because certain foreign investors are insensitive to the nature of the legal system in host countries. For example, Western investors may be more likely to be sensitive to legal systems that have a weak commitment to the rule of law, while Asian investors are likely to be less sensitive to these factors as they rely more on informal commitments and relationships.[32] Firms that are export-oriented may have less interaction with domestic law enforcement and therefore are less sensitive to the legal regime of the host country. Perry calls for more research into these conclusions,

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[27] Agnes Benassy Quere, Maylis Coupet and Theirry Mayer, "Insitutional Determinants of Foreign Direct Investment," (2007) 30 The World Economy 5.

[28] World Bank, *Doing Business in 2004: Understanding Regulation* (2004) (Washington, DC: World Bank), p. viii.

[29] Kevin Davis and Michael B. Kruse, "Taking the Measure of Law: The Case of the Doing Business Project," (2007) 32 Law & Social Inquiry 4 at 1095-1119.

[30] Amanda Perry, "Effective Legal Systems and Foreign Direct Investment: In Search of the Evidence," (2000) 49 International and Comparative Law Quarterly at 779-799.

[31] Ibid. at 789.

[32] Ibid. at 793.

but also cautions developing countries against spending scarce resources on legal system reform to court foreign investors who are insensitive to domestic legal systems.

There are still those who assume a much stronger cultural stance by rejecting any type of rationality behind individual behaviour. Lawrence Harrison, for instance, argues that laws and formal institutions do not change culture. It is necessary to modify culture before promoting legal and institutional reforms.[33] Harrison argues, for instance, that progress-resistant societies have the following cultural outlooks: they have religious beliefs that nurture irrationality, inhibit material progress, and are utopian; their views of destiny are informed by fatalism, resignation and sorcery; their members are focused on the present or on the past, not on the future, creating difficulty with planning and punctuality; wealth is conceived as a non-expandable resource and resource allocation is a zero sum game; knowledge is abstract, theoretical and cosmological, among other things. His argument is that these societies will not develop unless they change these cultural traits.[34]

While Harrison seems to strongly reject the idea that any law could promote development, there are Law & Development scholars that subscribe to a more concise and contextualized version of Harrison's claim. For example, Katharina Pistor, Antara Haldar, and Amrit Amirapu in a recent paper show that the status of women in society is relatively weakly associated with various Rule of Law indices and that in poor countries this association disappears altogether. They suggest that this occurs because the status of women in society is determined primarily by social norms about gender equality and that these norms are only weakly affected by legal institutions.[35] Unlike Harrison's claims, however, Pistor et al.'s paper can still be reconciled with the idea that law could promote development if we consider that some issues such as status of women in society might be more influenced by informal norms and social values, while norms relating to due process are not so heavily influenced by informal norms. Thus, formal institutional reforms might be more likely to change and modify informal rules and norms in certain cases, but might be a rather limited instrument in others.

These examples show how economics and social sciences can influence Law & Development in a variety of ways bringing a rich conceptual and methodological diversity among the scholars in the field.

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[33] Lawrence E. Harrison, *The Central Liberal Truth* (Oxford: Oxford University Press US, 2006).

[34] Ibid.; See also Samuel P. Huntington, Lawrence E. Harrison, *Culture Matters: how values shape human progress* (New York: Basic Books, 2000). For an overview of the growing influence of culture on the literature on Law & Development, see Amy J. Cohen, "Thinking with Culture in Law and Development", (2009) Buffalo Law Review 57 (2) at 511-586.

[35] Katharina Pistor, Antara Haldar, Amrit Amirapu, "Social Norms, Rule of Law, and Gender Reality", in James Heckman, Robert Nelson and Lee Cabatongian (eds.), *Global Perspectives on the Rule of Law* (London: Routledge, 2010).

In addition, post-modern and post-colonial theories that have influenced social sciences have also made their way into development studies to create what became known as post-development.

> Along with 'anti-development' and 'beyond development', post-development is a radical reaction to the dilemmas of development. Perplexity and extreme dissatisfaction with business-as-usual and standard development rhetoric and practice … are keynotes of this perspective. Development is rejected because it is the 'new religion of the West'…it is the imposition of science as power…it does not work…it means cultural Westernization and homogenization… and it brings environmental destruction. It is rejected not merely on account of its result but because of its intentions, its world-view and mindset. The economic mindset implies a reductionist view of existence. Thus, … ' it is not the failure of development which has to be feared, but its success.'[36]

The deconstruction of the concept of development and development discourse does not necessarily imply that we should be ready to accept any standard of living, thus becoming radical relativists. Rejecting developed countries' views of the developing countries is not an objection to the continued use of a critical analysis of underdevelopment. Indeed, this deconstructive exercise, in which one challenges conceptions of development presented by the Western world, may assist in the formulation of an alternative conception of development, not based on Western values (or at least not exclusively). Alternatively, it can also serve to ask whether there could be alternative strategies to deal with development problems (means of development) which are not necessarily based on mimicking Western institutions or Western culture.

Such critical claims are exemplified by what became known as the "Asian Way", which may refer to one of two claims. One version of the "Asian Way" offers an alternative to traditional conceptions of development by accepting one Western value (economic modernization), while rejecting others, such as those linked to liberal

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[36] J. Nederveen Pieterse, "After post-development", (2000) Third World Quartely 21(2) 175 at 175. Arturo Escobar, for instance, claims that the imperialistic nature of the development discourse makes it comparable to discourses of colonization: "The production of discourse under conditions of unequal power is what Mohanty and others refer to as 'the colonialist move'. (…) Although some of the terms of this definition might be more applicable to the colonial context strictly speaking the development discourse is governed by the same principles: it has created an extremely efficient apparatus for producing knowledge about, and the exercise of power over, the Third World." Arthuro Escobar, *Encountering Development: The Makind and Unmaking of the Third World* (Princeton: Princeton University Press, 1995) at 9.

democracies.[37] Another version of the "Asian Way" does not reject Western values in principle, but questions whether Western institutions are the only legitimate way of achieving and protecting these values. For instance, Daniel E. Bell proposes a bicameral representative democracy in which the upper house consists of members selected through examination. This proposal aims at combining democracy with the Confucian ideal of rule by the virtuous.[38] Bell's assumption is that institutions adapted to Asian values will have a better prospect of success in achieving these ideals.

These examples do not offer a comprehensive list of all possible methodologies used in this field, but it does illustrate that Law & Development is not a uniform and cohesive field of study. Scholars can diverge on their conceptions of development, disagree on how law relates to development, adopt distinct methodologies to analyze development problems, yet still be grouped under the same label, "Law & Development". What brings all these different perspectives and approaches together? The problem of development. Following in the footsteps of development studies, Law & Development uses many disciplines at hand to try to understand why there is persistent and systematic poverty and inequality in certain regions around the world. Thus, despite these methodological divergences, these scholars are united by one concern: how law can help or hinder the problem of development.

3. A Recent Trend: Law, Institutions & Development

The previous sections have shown that Law & Development scholars do not adopt one single concept of development, may disagree on the relationship between law and development, and do not adopt one single methodology in their studies. Given this conceptual and methodological diversity, it is almost impossible to provide the reader with an easy and quick overview of the main issues and questions addressed by Law & Development scholarship, while at the same time capturing the richness of all the different perspectives that are embraced by the label. Therefore, any reader searching for a quick introduction into the field needs to be mindful that any presentation will adopt a particular perspective that is not necessarily shared by or subscribed to by all Law & Development scholars. With this disclaimer, I will present one of these perspectives, which has gained increased importance in the last decade.

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[37] Inoue Tatsuo, "Liberal Democracy and Asian Orientalism," in Joanne R. Bauer, Daniel A. Bell, (eds.) *The East Asian challenge for Human Rights,* (Cambridge: Cambridge University Press, 1999) at 28. For instance, Asian leaders such as Singapore's Lee Kuan Yew have argued that some civil and political liberties are incompatible with values embedded in Asian culture. See Fareed Zakaria, "A Conversation with Lee Kuan Yew", Foreign Affairs 73 (2) March/April 1994.

[38] Tatsuo, supra note 37 (commenting on Daniel A. Bell, "A Confucian Democracy for the Twenty-First Century," presented at the international symposium on Asian legal philosophy, (University of Tokyo, October 10, 1996)).

Beginning in the 1990s, an institutional perspective on development has become increasingly prominent in development thinking. This institutional perspective was largely based on the work of new institutional economists, who assume that people respond to incentives and that many of these incentives are created by institutions. These new institutional economists often adopt Douglass North's definition of institutions, which is the following:

> Institutions are the rules of the game of a society, or, more formally, are the humanly devised constraints that structure human interactions. They are composed of formal rules (statute law, common law, regulation), informal constraints (conventions, norms of behaviour and self-imposed codes of conduct), and the enforcement characteristics of both. Organisations are the players: groups of individuals bound by a common purpose to achieve objectives. They include political bodies (political parties, the senate, a city council, a regulatory agency); economic bodies (firms, trade unions, family farms, cooperatives); social bodies (churches, clubs, athletic associations); and educational bodies (schools, colleges, vocational training centres).[39]

This definition distinguishes institutions from organizations, which create, apply and enforce the "rules of the game". Thus, according to this definition, property rights would be an institution, while the land registry and the police would be organizations.

Based on this definition, North (one of the founders of the new institutional economics) has argued that developing and transitional economies struggle because their institutions create incentives that are ill-suited for economic growth: "Third World countries are poor because the institutional constraints define a set of payoffs to political/economic activity that do not encourage productive activity."[40] These assumptions have been tested and a number of authors have now concluded that there is a strong empirical basis to support the idea that institutions do matter for development.[41] In

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[39] Douglass C. North, 'The New Institutional Economics and Third World Development' in John Harriss, Janet Hunter, and Colin M. Lewis, eds., The New Institutional Economics and Third World Development (London: Routledge, 1995) at 23.

[40] Douglass North, Institutions, Institutional Change and Economic Performance (Cambridge: Cambridge University Press, 1990) at 110.

[41] Dani Rodrik, Arvind Subramanian, & Francesco Trebbi, "Institutions Rule: The Primacy of Institutions over Geography and Integration in Economic Development" (2004) 9 J.Econ.Growth 131 at 141; A. Acemoglu, S. Johnson and J. A. Robinson, "The Colonial Origins of Comparative Development: An Empirical Investigation", American Economic Review (2001); A. Acemoglu, S. Johnson, and J.A. Robinson, "Reversal of Fortune: Geography and Institutions in the Making of the Modern World Income Distribution", Quarterly Journal of Economics 2002.

the development field, the assumptions of the new institutional economics were captured in the slogans "Institutions Matter," or "Governance Matters." Led by the Governance Group at the World Bank, systematic cross-country econometric analyses of the impact of institutional quality on development outcomes have been undertaken. The findings of this empirical perspective are exemplified in one particularly influential study entitled, "Governance Matters." This cross-country study was undertaken by Kaufmann, Kraay, and Zoido-Lobaton, all of whom are affiliated with the World Bank. This regularly updated study is part of the World Bank's ongoing research on governance which now covers almost 200 countries.[42]

The idea that "institutions matter" has prompted a massive surge in development assistance for institutional reform projects in developing and transition economies involving investments of many billions of dollars. Since 1990, the World Bank has spent $2.9 billion sin support of 330 rule of law projects.[43] "Institutions Matter" is, therefore, one of the most influential ideas in Law & Development thinking nowadays. This does not mean, however, that the Law & Development scholarship influenced by this idea does not have problems. The next section describes three of these problems, as described by Pranab Bardhan.[44]

3.1 What do we meant by institutions?

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[42] Daniel Kaufmann, Aart Kraay, and Pablo Zoido-Lobaton, "Governance Matters", World Bank Policy Research Working Paper No. 2196 (Washington DC: World Bank,1999) online: http://www.worldbank.org/research; Daniel Kaufmann, "Rethinking Governance: Empirical Lessons Challenge Orthodoxy" Discussion Draft 11 March 2003 (Washington DC: World Bank, 2002) online: http://www.worldbank.org/wbi/governance/pdf/rethink_gov_stanford.pdf; see also Daniel Kaufmann, Aart Kraay, and Massimo Mastruzzi, "Governance Matters IV: Governance Indicators for 1996-2004" World Bank Policy Research Group Working Paper No. 3630 World Bank2005, online: http://www.worldbank.org/wbi/governance/pdf/GovMatters_IV_main.pdf; Daniel Kaufmann, Aart Kraay, and Massimo Mastruzzi, "Governance Matters VII: Aggregate and Individual Governance Indicators, 1996-2007" World Bank Policy Research Working Paper No. 4654 (Washington DC, World Bank, 2008), online: http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1148386; World Economic Forum, Daniel Kaufmann, "Governance Redux: The Empirical Challenge" in Xavier Sala-i-Martin, ed., *The Global Competitiveness Report 2003-2004*, (New York: Oxford University Press, 2004). See also World Bank, *Where is the Wealth of Nations? Measuring Capital for the 21st Century* (Washington DC: World Bank, 2007).

[43] David Trubek, "The Rule of Law in Development Assistance: Past, Present and Future," in Trubek & Santos, *New Law and Economic Development, supra* note 8 at 74.

[44] Pranab Bardhan, "Law and Development", in A.K. Dutt and J. Ros (eds.), *International*

Handbook of Development Economics, vol. II (Cheltenham, UK; Massachussets, USA: Edward Elgar, 2008). For a more detailed analysis, see Davis and Trebilcock, supra note 8.

The first problem is definitional in nature: there is no consensus on how certain institutions should be understood. We know that institutions matter, rule of law matters and security of property rights matter, but what exactly we mean by each of these concepts is not very well defined. As Bardhan explains

> what is often ignored in this literature is that the 'rule of law' involves actually a whole bundle of rights, and we need to 'unbundle' it. Even for security of property rights, different social groups may be interested in different aspects of these rights. For example the poor may be interested primarily in very simple rights like land titles, and also, to a very important extent, in protection against venal government inspectors or local goons; to them that is the most salient aspect of security of property rights. For the richer investors, however, a whole range of other issues like protection of the minority shareholders in corporations, oversight of capital markets against insider abuse, bankruptcy laws, etc. loom large; these are what investors emphasize when they talk about security of property rights.[45]

And Bardhan is not alone in voicing this concern. Many scholars have also pointed out to the lack of precision of the term "rule of law". Dani Rodrik asks: "am I the only economist guilty of using the term [rule of law] without having a good fix on what it really means? (…) Well, maybe the first one to confess to it."[46] It is important to note that this is not merely a conceptual problem: without knowing what we are looking for, it is hard to design effective reforms for development.

3.2 Why do Developing Countries not Change Bad Institutions?

The second problem is the persistence of bad institutions in developing countries. As Bardhan explains,

> a central issue of development economics is thus the persistence of dysfunctional regulations and institutions over longs periods of time (…) In particular, the history of underdevelopment is littered with cases of formidable institutional impediments appearing as strategic outcomes of distributive conflicts. (…) The classic example of inefficient rules and institutions persisting as the lopsided outcome of distributive struggles relates to the historical evolution of land rights in developing countries. In

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[45] Ibid. p. 2

[46] The Economist, *Order in the jungle: The rule of law has become a big idea in economics. But it has had its difficulties,* Mar 13th 2008.

> most of these countries the empirical evidence suggests that economies of scale in farm production are insignificant (except in some plantation crops) and the small family farm is often the most efficient unit of production. Yet the violent and tortuous history of land reform in many countries suggests that there are numerous road blocks on the way to a more efficient reallocation of land rights put up by vested interests for generations.[47]

The persistence of bad institutions in these countries also becomes evident in the failure of the many attempts to promote rule of law and institutional reforms in developing countries in recent decades. Michael Trebilcock and Ron Daniels show how reform efforts have thus far yielded mixed to disappointing results in numerous cases of attempted reforms in Africa, Asia, Latin America and Eastern Europe.[48] And they are not alone: others have called attention to the fact that significant resources have been employed to promote good governance in developing countries, but there are no significant signs of improvement.[49]

Possible reasons for the disappointing results thus far include three main obstacles to reforms.[50] First, despite political will to promote reforms, countries may lack the necessary financial, technological or human resources to implement changes. Second, a series of social values, norms, attitudes and practices, which Trebilcock and Daniels loosely classify as socio-cultural-historical factors, may form a hostile environment for implementing reforms.[51] Third, there are political-economy based impediments, described by Bardhan. Interest groups will resist reforms that eliminate their privileges, do not foster their interests, or otherwise do not offer any gains (material or otherwise). We can describe most of these obstacles and the self-reinforcing mechanisms that keep them in place as path dependence. Dealing with this is a tall order, but path dependence

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[47] Bardan, supra note 44, pp. 7-8.

[48] Trebilcock and Daniels, supra n. 15.

[49] Thomas Carothers, 'The End of the Transition Paradigm'(2002) 13 *J. Democracy* 5; Thomas Carothers, 'The Rule of Law Revival' (1998) 77 *For. Aff.* 95; Bryant Garth &Yves Dezelay, 'Introduction' in Yves Dezelay & Brian Garth, eds., *Global Prescriptions: The Production, Exportation and Importation of a New Legal Orthodoxy* (Ann Arbor: University of Michigan Press, 2002); Brian Tamanaha, *On the Rule of Law: History Politics, Theory* (Cambridge: Cambridge University Press, 2004); Tamanaha, Primacy of Society, *supra* note 2.

[50] Trebilcock and Daniels, supra note 15, at 39-40.

[51] Ibid. at 39. (there may be "social-cultural-historical factors that have yielded a set of social values, norms, attitudes, or practices that are inhospitable to even a limited conception of the rule of law.")

needs to be overcome in order for institutional reforms for development to start producing meaningful results.[52]

These obstacles not only make it difficult to conduct reforms, but they actually raise doubts as to the strength of the case for these reforms. It may well be the case that the costs generated by institutional reforms in terms of social disruptions, political costs, and financial resources consumed may surpass the actual benefits of moving from a "less functional" institutional framework to a "more functional" one. Formalization of property rights, for instance, has gained a lot of traction recently, due largely to the work of Hernando de Soto.[53] But the case for formalization is not as strong as it seems, because the costs of creating a formal property rights regime in certain cases outweigh the benefits derived from that same regime.[54]

Ultimately, the new institutional economists can safely claim that institutions matter for development, but they do not know how to reform them. The inability to promote successful institutional reforms is therefore one of the main problems now confronting the development agenda.

3.3 Does Good Governance Means the Same Thing for All Countries?

The third problem identified by Bardhan is that this literature

> may need to change or made more flexible if it is to be applied to developing countries. One relates to the scale of economic activity. In small peasant communities where the scale of economic activity is not large, informal relational contracts may be more efficient than rule-based contracts supported by elaborate legal-judicial procedures. Breaches of relational contracts are often observable by other community members even when not verifiable by courts, and punishment is usually through social sanctions and reputation mechanisms. Another advantage is flexibility and ease of renegotiation. But as the scale of economic activity expands, as the need for external finance becomes imperative, and as large sunk investments increase the temptation of one party to renege (and as

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[52] Mariana Prado & Michael Trebilcock, "Path Dependence, Development, and the Dynamics of Institutional Reform", 2009 University of Toronto Law Journal 59 (3) at 341-380.

[53] Hernando de Soto, *The Mystery of Capital: Why Capitalism Triumphs in the West and Fails Everywhere Else,* (New York: Basic Books, 2003).

[54] Michael Trebilcock and Paul-Erik Veel, "Property Rights and Development: The Contingent Case for Formalization", 2008 University of Pennsylvania Journal of International Law 30 (2) at 397- 481.

> increased mobility and integration increase the outside world improve exit options), relational contracts and reputational incentives become weaker.[55]

Bardhan's concerns are illustrated by the so-called 'China Enigma' and the 'East Asian Miracle.' In both of these cases, high rates of economic growth have been achieved, often in the absence of strong formal contract law and enforcement regimes. This may suggest that much economic development is realizable through informal contracting mechanisms.[56] This is not to say that contracts do not matter. Trebilcock and Leng argue that

> at low levels of economic development informal contract enforcement mechanisms may be reasonably good substitutes for formal contract enforcement mechanisms, but become increasingly imperfect substitutes at higher levels of economic development involving large, long-lived, highly asset-specific investments or increasingly complex traded goods and services, especially outside repeated exchange relationships. [57]

However, many developing countries may not be at this stage, and therefore may not derive as many economic benefits from contract law as new institutionalists sometimes suggest.

In general, economists can be accused of not paying enough attention to culture as a relevant factor in human behavior, and of not acknowledging its relevance for the development process. [58] Paradoxically, there is one important exception within this group: the new institutional economists,[59] who follow for the most part Douglass North's definition of institutions, which includes formal rules (statute law, common law, regulation) and informal constraints (conventions, norms of behaviour and self-imposed codes of conduct).[60] Informal and relational contracts described by Bardhan are encompassed by what North calls informal institutions. Thus, according to the new

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[55] Bardhan, supra note 44, at 11.

[56] Michael J. Trebilcock and Jing Leng, "The Role of Formal Contract Law and Enforcement in Economic Development" *Virginia Law Review,* Vol. 92, pp. 1517-1580, 2006.

[57] Ibid.

[58] Amartya Sen, "How Does Culture Matter?" in Rao & Walton (eds.), supra note 4 at 37.

[59] And according to Sen they are not the only ones. Adam Smith, Jonh Stuart Mill and Alfred Marshal can alsobe cited as examples.

[60] North, supra note 40 and accompanying text. Another example is North's most recent book, Douglass C. North *Understanding the Process of Economic Change* (Princeton: Princeton University Press, 2005).

institutional economics these informal norms (also called culture), together with formal institutions, influence human behaviour and structure social interactions.

The problem is that institutional economists do not go much beyond acknowledging that culture influences human behaviour. It is not clear how, when and why culture does so. The result is that culture is often treated as a black box in institutional analyses.[61] We do not know, for instance, to what extent the existence of formal institutions, such as rule of law and democratic accountability depends on certain underlying cultural values, such as individualism and lack of hierarchical structures.[62] We also do not know if formal institutions can change culture and vice-versa.[63] And if these changes are possible, we do not know when and under which circumstances they are likely to take place.

This poses a major obstacle for the advancement of our understanding of the problem of development. As I have shown, institutional theories of development have become prominent in the last decade or so, and many development efforts are currently motivated by the assumption that institutions matter for development. However, without a thorough assessment of the role that culture plays in institutional stability and institutional change, reforms may have either limited success or unintended results. Culture is an important factor that is currently largely missing in the institutional reform puzzle.

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[61] Acemoglu, D. and Johnson, "Unbundling Institutions," (2005) 113 *Journal of Political Economy* 5.

[62] For an analysis suggesting that there is empirical evidence to support the idea that there is significant influence of culture on governance, see Amir Licht, Chana Goldschmidt, and Shalom Schwartz, "Culture Rules: the Foundations of the rule of law and other norms of governance," (2007) 35 *Journal of Comparative Economics*, p. 659-688.

[63] Harrison, for instance, argues that formal institutions do not change culture. It is necessary to modify culture before promoting institutional reforms. Lawrence E. Harrison, *The Central Liberal Truth* (Oxford University Press US, 2006).

Conclusion

This article presented a brief introduction to "Law & Development" by analyzing three aspects of this field: (i) how scholars relate law to development; (ii) what kind of methodologies these scholars adopt; and (iii) recent trends.

First, regarding the relationship between law and development the article suggested that scholars can be mostly divided in two groups: those that see law as an instrument of promoting development (*law in development*) and those that see law (rule of law) as an end in itself and one of the goals that should be pursued by development reforms (*law as development*). The first group can be subdivided further into two groups: those that subscribed to strong state intervention in the economy, conceiving law as an instrument to implement governmental policies (law in the developmental state) and those that subscribe to neoliberal theories of development, and believe that law should only create the conditions for the invisible hand to work its magic by enforcing contracts and protecting property rights (law in the neoliberal state).

The main distinction between *law in development* and *law as development* is the concept of development adopted by these theories. While the first is closely attached to the idea of development as economic growth, the second is influenced by Amartya Sen's concept of development as freedom. In suggesting that law can be both an end and a means to achieve development, this concept brings these two groups closer together, implying that the distinction presented above may be too sharp.

Second, regarding the methodologies adopted by Law & Development scholars, this article has suggested that there are many and it is hard to present a comprehensive list of all of them. Much like the interdisciplinary field of development studies, Law & Development has been influenced by economics and social sciences, such as sociology and anthropology. These methodological differences can easily turn into substantive disagreements in the field. For instance, scholars that adopt strong economic assumptions (individuals are rational self-interested actors that respond to incentives) tend to believe that law is a very effective tool for modifying human behaviour. On the other hand, scholars who are more open to social sciences and therefore believe that social dynamics and individual behaviour are not solely guided by economic rationality question the law's potential to effectively promote social change.

Third, regarding recent trends, the article introduces the idea that "institutions matter" or "governance matters". These mantras capture one of the most prominent assumptions in development thinking today, informing a great deal of the investments in reforms promoted by multilateral organizations such as the World Bank. Despite being informed by the robust theoretical framework of the new institutional economics, and being supported by a significant amount of empirical data (quantitative studies), this

institutional trend in "Law & Development" has problems. First, the field needs to account for the different meanings and aspects of each institution that it claims to be conducive to development. For instance, what protection of property rights means for rich people may be very different from the property rights agenda for the poor. Second, even if we accept to the conclusion that institutions matter, but we do not know how to change them. Developing countries are still plagued by bad institutions, which persist despite significant efforts to change them. Finding ways to deal with path dependence and other obstacles for reform is one of the most pressing challenges for the institutional perspective. Third, different institutions may be necessary at different levels of development. Informal institutions may be more relevant at lower levels and formal institutions may only become relevant above a certain development threshold. If this is the case, the institutional perspective needs to develop a better grasp on how these informal rules work, what role they play, and how they interact with formal institutions over time. Without opening the black box of culture, the institutional perspective seems to be missing an important piece of the development puzzle.

In sum, Law & Development scholars do not adopt one single concept of development, may disagree on the relationship between law and development, do not adopt one single methodology in their studies. Even if these scholars seem to be currently converging somewhat into a consensus around the idea that "institutions matter", there is still much work to be done in this area for this institutional perspective to become a workable and effective one. Without an answer to the three problems identified above, one is left without an answer to the quest for a solution to end world poverty. And until that answer is found, Law & Development scholars will continue searching, being open to anything that may be potentially useful to ensure that every individual can choose to live the life that they have a reason to value. ■