THE ECONOMIC ANALYSIS OF LAW - WILL THE ROMANIAN DOCTRINE FINALLY CATCH UP WITH IT?

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Abstract
Although a well-established presence on the international legal scene, the economic analysis of law is still an unfamiliar concept to most Romanian scholars. While worldwide, prestigious universities offer special courses on this topic and an impressive body of legal studies continues to add up, only scant traces of this important legal school can be detected in some recent Romanian doctoral thesis and papers.
This article explores the main concepts of the economic analysis of law, the recent spin-offs of this theory, especially in the area of comparative law, as well as some of the critiques addressed in the legal doctrine, concerning the consequences on law of overemphasizing "efficiency" to the expense of less quantifiable, moral and social considerations. Some explanations on why the Romanian doctrine is lagging behind with respect to the economic analysis of law will also be attempted, together with a tentative answer to whether this major legal theory will ever make an impact on local doctrinal developments in the near future.

Key words: *economic analysis of law, efficiency, legal origins thesis, comparative law, legal reform*

Introduction

The economic analysis of law as developed by the Chicago school in the early 1960s can trace its origins to various preceding theories – like American realism and utilitarianism - that shaped the western legal thought long before concepts such as market economy, efficiency, transaction costs (terminology specific to this doctrine) and law as instrument for promotion of economic efficiency, could be coherently developed in one unifying theory. The impact of this doctrine that purports to measure the efficiency of legislation and court decisions with the conceptual tools provided by economics has not been negligible in common-law systems, mainly in USA, its country of origin, where traditionally positivism has held a preeminent place, with its emphasis on the autonomy of law and its legal phenomena. The latest spin-offs of the economic analysis of law can be found in the comparative law field, namely in the legal origins theories, that link economic performance to certain characteristics of a legal system, implying that some systems are better suited to economic development than others.

As stated in the abstract, this paper presents summarily the main concepts of the economic analysis of law, in order to better assess its today impact on the comparative law field. The paper also reviews the very few Romanian works that deal with the issue of law and economics (an alternative name for the economic analysis of law), even though two of these works are purely philosophical-speculative and hence have more to do with political economy than law. The scarcity of Romanian research on this topic highlights what we believe to be a certain cultural aversion towards such a realistic, harsh approach to law, aversion shared in fact by the many legal cultures from the continent.

Moreover, even our most comprehensive compendia on philosophy of law or jurisprudence[1] and its historical developments do not include the economic analysis of law in their presentation. Therefore, we consider that a research paper on this matter, that reviews not only the main theory, but also its current avatars in the legal field, will prove useful by the relative novelty of this theme in our

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[1] One of the most notable contribution on this subject is made by "The Philosophy of Law: Major Legal Theories", ("*Filosofia dreptului. Marile curente*") by N. Popa, I. Dogaru, Gh. Dănişor, D.C. Dănişor, ed. ALLBECK, Bucharest, 2002.

legal doctrine, and will perhaps spur an interest in the economic analysis of law that will go beyond narrowly-focused research papers on tort liability and collateral securities or speculative doctoral thesis in philosophy and political economy.

1. Brief presentation of the economic analysis of the law theory

In introducing this topic, some authors formulate the issues this theory purports to answer, such as "should law be primarily concerned with promoting economic efficiency?"[2] This theory is not politically-neutral, so "the answer will depend upon the political leaning of the reader. The believer in the free market and *laissez-faire* economics will answer the affirmative, whereas the more left-leaning individual will counter that law should be more about justice, rights and redistribution.(…) despite the fact that judges, lawyers and individuals appear to view the law in terms of rights and justice, there is a school of legal thought which not only advocates that the law ought to be concerned with economic efficiency, but also claim to put forward a descriptive theory in which law is concerned with promotion of economic efficiency and the protection of wealth as a value"[3].

This theory originates with the publication in 1960 by the economist Ronald Coase of the now famous article "The problem of Social Costs"[4] and uses economic concepts such as "efficiency" and "transaction costs" in conjunction with socio-legal concepts, such as "distribution of wealth", "equity", "allocation of rights" to assess the consequences of legal rules in practice. In a widely quoted book on this subject, "An Introduction to Law and Economy"[5], A.M. Polinsky defines *efficiency* as the relationship between the aggregate benefits and the aggregate costs of a situation (viewed in simplified terms of monetary loss or gain), while the term *equity* concerns the distribution of income among individuals, or "in other words, efficiency corresponds to the "size of the pie", while equity has to do with how it is sliced"[6]. Another concept advanced by R.H. Coase refers to the *transaction costs*, that include the costs of identifying and getting together with the parties one has to negotiate a particular situation, the costs of the negotiation process itself and the costs of enforcing the result of such negotiation. Initially, in his article Coase dealt with a specific theme, that of assessing those activities of business firms which have harmful effects on others[7] and the allocation of liability damages, drawing on a number of tort and nuisance cases adjudicated by the English courts. Challenging the conventional economic and legal wisdom that polluter has to pay, Coase brings a different angle to the classic dilemma: if A has inflicted harm on B, how should one restrain A (one of the examples given is that of confectionery maker whose noisy operating machine disturbs a practicing doctor). In this example, the choice is whether the confectioner should not be allowed to operate a noisy machine to make confectionery or the doctor should not be allowed to carry on with his practice. Coase suggests that this situation involves reciprocity and that the real question is whether A should be allowed to harm B or B should be allowed to harm A. This means that the initial allocation of rights (by courts or by law) might produce a different economic result, in a real world where transaction costs are positive (are not zero). The answer to this dilemma, Coase

[2] H. McCoubrey & Nigel D. White, "Textbook on Jurisprudence", Oxford Univerity Press, 3rd ed., 1999, p. 275.

[3] Idem 3, p.275.

[4] R.H. Coase, "The Problem of Social Costs", Vol. 3 Journal of Law and Economics, p. 1-44. The article is available online at: http://www.colorado.edu/ibs/eb/alston/econ4504/readings/Coase,%20The%20Problem%20of%20Social%20Costs.pdf.

Ronald H. Coase is a 1991 Nobel Laureate in Economics "for his discovery and clarification of the significance of transaction costs and property rights for the institutional structure and functioning of the economy."

[5] A. M. Polinsky, "An Introduction to Law and Economy", Wolters Kluwer, Law & Business, 4th edition, New York, 2011.

[6] Idem 6, p. 7.

[7] Idem 5, p. 1.

contends, lies in a cost-benefit analysis that should be taken into account by judges when adjudicating allocation of rights (and implicitly allocation of income), the transaction costs for each party being evaluated against the increase/decrease in the value of production, i.e. against value maximization. In the example above, the problem was if it was worthwhile to secure more doctoring at the expense of the diminished production of confectionary. According to what is referred to as Coase Theorem, "if there are positive transaction costs, the efficient outcome may not occur under every legal rule. In these circumstances, the preferred legal rule is the rule that minimizes the effects of transaction costs"[8]. Consequently to the publication of this article, the concept of wealth maximization assumes a central role for all ensuing theories based on Coase's work.

The concepts outlined above have been developed by many a scholar, creating different approaches within the economic analysis of law. The contributions of Calabresi and Melamed[9] in the field of tort liability and that of Richard Posner are the most significant in this respect. Calabresi has addressed some of the shortcomings of the Coase's analysis by moving the discussion away from the efficient outcome of a dispute between two parties and steering it towards the decisions that society through it legislative bodies has to make as to the nature of a right (entitlement) and its distribution. According to Calabresi, "the first issue which must be faced by any legal system is one we call the problem of 'entitlement'. (…) Hence the fundamental thing that law does is to decide which of the conflicting parties will be entitled to prevail. The entitlement to make noise versus the entitlement to have silence, the entitlement to pollute versus the entitlement to breath clean air (…) these are first order legal decisions"[10]. Entitlements can be those protected by a simple property rule (negotiated by individuals), those bought and sold at a price determined by the state (governed by so-called liability rules) and entitlements that are inalienable or that can be sold only under specific conditions (governed by inalienability rules). The authors list three groups of reasons for deciding in favor of one entitlement over the other: "economic efficiency, distributional preferences, and other justice considerations"[11]. Calabresi and Melamed make the case for entitlements protected by liability rules rather than property rules on the basis of their economic efficiency and claim that their analysis is a working framework for legal decision in tort liability cases. Their theory does allow aspects of justice into their economic-based approach, in terms of distribution of entitlements and of their designation as to which are to be protected by liability or inalienability rules[12], but their analysis is still centered on the issue of economic efficiency in a functioning free market economy.

Richard Posner is perhaps the most well-known exponent of the law and economic movement. In his seminal works, "Economic Analysis of Law", "The Problems of Jurisprudence" and "The Economics of Justice", Posner links the common-law bias for promotion of efficiency to the free-market principles that govern the Western countries and thus explains the judicial tendency to arrive at conclusions that maximize wealth. Posner contends that common-law judges do tend to base their decisions on efficiency considerations and provides a list of subject-matters where such decisions are well documented, especially in the contract law, property law and tort law. How these considerations apply to other legal field it is less clear, though, and represents one of the vulnerabilities of his theory. Posner does not limit the economic analysis of law merely to a descriptive tool for evaluating law, but purports to impose a normative dimension as well, stating that a few economic principles can be applied as formulas to the legal field and that judicial decisions could be evaluated against the overriding aim of wealth maximization, conceptually based on the model of voluntary market transactions. As was noted in the beginning of this section, this theory is

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[8] Idem 6, p.15.

[9] The most quoted article refers to "Property Rules, Liability Rules and Inalienability: One View of the Cathedral" by G. Calabresi and A.D. Melamed, (1972),Vol. 85 Harvard Law Review, p. 1089-1128, available in pdf format at: www.amherst.edu/media/view/123372/original/CalabresiMelamed.PDF.

[10] Idem 10, p.1090.

[11] Idem 10, p.1093.

[12] Idem 3, p. 282.

not politically-neutral, being steeped in a particular economic model, that promotes a minimal state intervention in the economy, that "rewards the traditional 'Calvinist' or 'Protestant' virtues and capacities associated with economic progress"[13] and is based on an unflinching belief in the self-regulatory forces of the free market.

The economic analysis of law has drawn widespread criticism from the more traditional legal scholars. The issues raised against this theory range from its failure to explain (with the possible exception of Calabresi) the initial allocation of rights in society to its sweeping assumptions that men operate solely for the purpose of wealth maximization or that wealth is a social value by itself, unrestrained by other considerations. The contention by Posner that "common-law is best (not perfectly) explained as a system for maximizing the wealth of the society. Statutory or constitutional as distinct from common-law fields are less likely to promote efficiency (…)"[14] points to its preference for common-law rules over state regulation. His opinions on the common-law legal system as a system that maximizes wealth have been taken over by a new generation of economists and, to a lesser extent, by jurists enthralled by the simplicity of the main tenant of the economic analysis of law school, that law should promote economic efficiency. The ensuing theories have impacted law in many an unpredictable way, affecting even those disciplines that traditionally escaped the scrutiny of economists or the imposition of economic influences, such as the comparative law.

2. The "legal origins" thesis – a 21st century avatar of the economic analysis of law

As was the case with the economic analysis of law, the legal origins thesis was initiated by a couple of economists borrowing core concepts from the field of comparative law, such as the classification of legal systems in civil and common-law systems, legal transplants and the function of law, and applying them to their own economically-focused analysis. This theory, whose main tenant claims that the common-law fosters economic growth better than the civil law, has proved to impact not only legal studies, but political and economic decisions worldwide, through its incorporation in the highly influential *Doing Business* reports issued by the World Bank.

The legal origins thesis can trace its beginnings to the work of a small number of economists, whose research focused initially on investor protection, namely Rafael La Porta, Florencio Lopez de Silanes, Andrei Shleifer and Robert Vishny, collectively referred to either as LLSV or LLS[15]. Believing in the transformational power of law as a tool to spur economic reform[16], LLSV set out to demonstrate the impact of good laws on development and in particular on economic growth. Since "good law" is not easily separated from the very fiber of society in which it operates so as to establish a causal link between good law and prosperity, and hence is not easily quantified, LLSV introduced a novel approach to this matter, analyzing those systems where the law was imposed exogenously, mainly through colonization by various European countries, and observing which country performed better in economic terms. This approach led them to the conclusion that legal origins matter[17], i.e. that countries with common-law systems performed better than those with civil law origins, due mainly to the fact that common-law systems are perceived to enjoy a greater degree of judicial independence from the executive compared to their civil law counterparts, and to its perceived adaptability to change, as a direct consequence of its limited reliance on codified law. In

[13] R. A. Posner, "The Economics of Justice", Harvard University Press, Cambridge, Massachusetts, 1981, p.68.

[14] R. A. Posner, "Economic Analysis of Law", 3rd ed., Little, Brown & Company, Boston, 1986, p.21.

[15] Ralf Michaels, "Comparative Law by Numbers? Legal Origins Thesis, *Doing Business* Reports, and the Silence of Comparative Law", vol. 57 The American Journal of Comparative Law, p.768.

[16] For some interesting historical insights on the idea that law is essential to economic development, see article by Curtis J. Milhaupt, "Beyond Legal Origins: Rethinking Law's Relationship to the Economy – Implications for Policy", vol. 57 The American Journal of Comparative Law, p. 831-832.

[17] Idem 16, p.769.

the wake of the enormous success this theory enjoyed, but also faced with a similar degree of criticism, the authors refined and expanded their theory beyond the investor protection field to encompass company law, bankruptcy law, labor laws and judicial independence. In essence, like its predecessor – the economic analysis of law, this theory is not politically-neutral, but is heavily influenced by the neoliberal political economy ideas prevalent in the decade spanning from the onset of the Asian crisis in 1998 to the 2008 global financial crisis (still influential, though to a lesser extent, today). It has been noted that countries hit by the global financial crises have all been given by international financial organizations a "fairly standard menu of legal reforms. The components of this menu, emphasizing shareholder rights and creditor protections and drawn predominantly from the US legal system, were influenced by the recent economics scholarship linking favorable economic outcomes to 'good' law. Since common-law regimes score well in this research, for many policy makers, 'good' has, not implausibly, meant Anglo-American (typically U.S.) law."[18]

As mentioned above, the main tenants of the legal origins thesis have made an impact on the international economic policies, through their incorporation by the World Bank in its *Doing Business* reports since 2002. "Beginning in 2004, the International Finance Group (IFC), a member of the World Bank Group, has been issuing reports that measure and compare the 'ease of doing business' in more than 130 countries worldwide. (…) the reports rely strongly (though not, of course, exclusively) on the legal origins thesis and its literature"[19]. Aimed at an international audience, these reports carry a different weight from the descriptive and analytical values of the legal origins thesis, introducing a quasi-normative perspective through its ranking of countries based on various benchmarks that purport to measure the attractiveness of a legal system for investment[20]. The main goal of these reports is to induce legal reforms in countries perceived to be deficient as to the ease of conducting business. Consistent with the legal origins theory, the top performers in this field belong to the common-law system, while civil law countries are lagging behind. Only Scandinavian countries and, lately, Germany, manage to make it to the top 10. In the 2012 report, for instance, the best performers were Singapore, Hong Kong and New Zealand, all countries with a common law system[21]. Since its first publications, countries engaged in a strong competition to improve their rankings, though the actual impact of the legal steps they took to make their business environment more investor-friendly is hard to evaluate in practice – perhaps by measuring the amount of new investment attracted by those reforms. Much criticism have been directed against these reports, ranging from its methodology and gathering of data, to the more substantive one "directed against perceived preferences for deregulation over other values – one being solidarity and justice, the other being culture"[22]. Another criticism have been directed towards the insufficient understanding of the law, either by misunderstanding or oversimplifying some traditional comparative law concepts, such as the division of legal families in civil and common law systems (selecting just two from all existing legal families) or by sheer ignorance as to the way legal transplants operate. The legal reform cannot be viewed in the simplistic terms of a legislation graft that will automatically induce economic growth.

The most vocal critique of the first *Doing Business* report have undoubtedly been voiced by the French legal profession, academics and leading practitioners alike, who joined forces in defending the values and merits of their civil law tradition, by establishing work groups, publishing

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[18] Idem 17, p. 832-833.

[19] Idem 16, p.771.

[20] For the most recent *Doing Business* report and the ranking methodology, see http://www.doingbusiness.org/rankings. For Romania, the country profile, contributors to the report and other relevant information can be accessed at the following address: http://www.doingbusiness.org/~/media/giawb/doing%20business/documents/profiles/country/ROM.pdf

[21] Romania is ranked at 72 in the list (out of 185 countries), behind Trinidad and Tobago or the Kyrghiz Republic, but ahead of Italy. France is ranked at 34. For more information on the 2012 report, idem 21.

[22] Idem 16, p.773.

papers and making direct appeals to the World Bank institutions. The French reaction to the *Doing Business* reports with its implicit statement that common-law is better than civil should be, in our opinion, of great interest for the Romanian legal profession as well, and highlights some common issues. After the publication of the first *Doing Business* report, the president of the Cour de cassation has officially declared that "French law was thus brutally reminded of the requirement of efficiency by American schools of economic analysis of economic development factors"[23]. The discontent of the French with the assumptions and conclusions of the report have been explained as stemming from cultural factors, such as the difficulty for a country with a strong tradition of exporting law to accept legal transplants or by the unease with the values that underpinned the report, which seemed foreign to those on which French legal system is built[24]. The response of the French legal professions has been vigorous and constructive, with a mixture of well-argued critique against the reports and its underpinning legal foundations (i.e. the economic analysis of law and the legal origins thesis) and research projects centered on the economic efficiency of law. It has been noted that before the publication of the reports, these two theories were only marginally considered by the French academics, because the "idea of economic performance of law, which underpins an economic analysis, thus stands in contrast to the humanistic approach, characteristic of civil law systems"[25]. The French scholars and practitioners have so rapidly mobilized also in recognition of the increased global competition that unavoidably extends to the market for legal services and have benefitted from the support of leading politicians, including the former French president, Nicolas Sarkozy.

To summarize the main points of this incursion in the odyssey of the economic analysis of law and its modern avatar, the legal origins thesis, it seems that a consensus between legal scholars emerges on the deficiencies and on the benefits of these economic approaches. It would be undoubtedly useful if these approaches could be employed by comparatists in conjunction with the more traditional analysis of law, so as a broader, more comprehensive and accurate picture of a particular legal system could be generated and hence particular legal reforms could have a better chance of success.

3. The economic analysis of law and its reflection in the Romanian legal doctrine

The most accurate thing one could say about this subject is that the economic analysis of law is conspicuous by its absence, with the few exceptions of some recent doctoral thesis and articles, not all of them in the legal field. While researching this paper, I discovered very few Romanian sources, which will be mentioned below in a (hopefully) non-exhaustive manner.

A compendium of current political philosophy schools of the right side of the political spectrum contains two articles, on the economic analysis of law and, respectively, on the Austrian school of law and economics[26]. Another source would be the published doctoral thesis of one of the editors of the previously mentioned compendium, called "The Privatization of Justice"[27]. Its scope

[23] Bénédicte Fauvaque-Cosson and Anne-Julie Kerhuel, "Is Law and Economic Contest? French Reactions to the Doing Business World Bank Reports and Economic Analysis of Law", vol. 57 The American Journal of Comparative Law, p.812.

[24] Idem 24, p. 815.

[25] Idem 24, p. 826.

[26] "Dreapta Intelectuală.Teorii şi şcoli de gândire ale dreptei contemporane occidentale" (*The Intellectual Right Wing. Theories and Schools of the Contemporary Right wing of the Political Spectrum*), editors: Ionuț Sterpan and Dragoş Paul Aligică, ed. Humanitas, Bucharest, 2011; the articles are "The Economic Analysis of Law", by Emanuel-Mihail Socaciu p. 279-291, and "The Austrian School of Law and Economics", by Mihai-Vladimir Topan and Tudor Smirna, p. 293-308. According to their résumés, none of these authors have legal training, and their articles do not go beyond the scope of the compendium, which is to broadly present current political theories.

[27] "Privatizarea justiției" (*The Privatization of Justice*) by Ionuț Sterpan, ed. Ars Docendi, Bucharest University, 2012.

includes not only the economic analysis of law, but also extends to the theory of Robert Nozick on the role of the state and the extent of its legitimacy.

Finally, in the legal field, the economic analysis of law takes a central role in a fairly recent research paper on security interests in personal property[28], and - according to the author - is touched upon in some other Romanian works on property rights and contractual obligations[29]. It does not follow that the concepts of economic analysis of law were explicitly assumed by those legal scholars or, indeed, that the theory is even mentioned by them, but rather that the way they conducted their research agrees with the spirit of the economic analysis of law. In his article "*Security Interests in Personal Property: A Necessary Evil of a Useful Tool*?"[30], the author contends that economic analysis of law is no strange concept to the Romanian courts, which since the end of 1990s onwards chose to liberally interpret some legal provisions regarding secured interests and credit operations in order to help the banks recover non-performing debts more quickly and to extend them a better legal protection against fraudsters[31].

The most visible and uncontroversial application of the economic analysis of law in Romanian legal field is the creation of the (now repealed) legislation governing the secured interests in personal property, namely Law no. 99/1999. As noted by the author, the rationale behind its adoption was pure economic consideration. Moreover, the drafting of this legislation was entrusted to an American organization, called CEAL - Center for Economic Analysis of Law. "The drafting process was a particular one, whereas a private body (CEAL) from a foreign state (USA) has drafted the proposed Bill, which was later translated into Romanian language, hurriedly amended and passed through Parliament by the special procedure of Government assuming its political responsibility"[32]. The acknowledged aim of this legislation concerned the promotion of economic efficiency through simplified, less costly procedures for secured interests in personal property.

4. Conclusions

The sketchy section on the Romanian legal doctrine concerned with the economic analysis of law presented above mirrors closely the current lack of interest by the Romanian scholars in a legal development that has been around for several decades and continues to grow in influence due to the economic globalization. Unlike their French counterparts, our academics and practitioners do not have a tradition of legal export to defend, but rather a tradition of legal imports to assess. More often than not, the Romanian laws were a copy-paste (and sometimes a poorly translated copy-paste) of legal rules from other systems, than a coherent attempt to make the legal transplants successful.

The reasons behind this disinterest are manifold. On one hand, there is a cultural motivation, which can be traced to the legal origins of our law system – the French civil law, with its deeply held belief that law should be about justice, fairness, social harmony, and less about efficiency. On the other hand, efficiency cannot be pursued strictly in the legal field and court decisions alone, it has to permeate all aspects of society. An indicator of the efficiency of the legal rules and their impact on

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[28] "Garanțiile reale mobiliare: un rău necesar sau un instrument util?" (*Security Interests in Personal Property: A Necessary Evil of a Useful Tool?*), by Radu Rizoiu, in Revista Română de Drept Privat nr. 3/2010, ed. Universul Juridic, Bucureşti.

[29] The author lists 2 such books: one on property rights - "Tratat de drept civil. Drepturi reale principale" (*Treatise on Civil Law. Property rights*), by O. Ungureanu, C. Munteanu, ed. Hamangiu, Bucureşti, p. 150-152, and the other on the general theory of contract – "Tratat de drept civil. Obligațiile" (*Treatise on Civil Law. Obligations*), vol.II, by L. Pop, ed Universul Juridic, Bucureşti 2009, p. 379-381, "Garanții reale mobiliare în dreptul comparat" (*Secured Interests in Personal Property – A Comparative View*), by Alandar Sebeni, doctoral thesis, University of Bucharest, 2005.

[30] Most of the ideas of this article were later included in his doctoral thesis on "Secured Interests in Personal Property", University of Bucharest, 2011.

[31] Idem 29, p. 166. Several court decisions are mentioned in this respect, such as Supreme Court of Justice (SCJ) decision no. 507/12.02.1998, SCJ decision no. 2536/16.06.1998, SCJ decision 5117/28.12.2005, etc.

[32] Idem 29, p. 237; translated from Romanian by the author of this paper.

economic development might lie in the stability/instability of a particular legal system. In fact, this would constitute an interesting application of the efficiency criterion to the Romanian law. Our legal system is characterized by a high degree of instability and our policy makers do not seem inclined to implement accurate measurement tools to assess the costs of this legislative instability on economic growth. Thus, the incentives for Romanian academics to engage locally in a meaningful debate on the economic theories are rather insignificant.

As to the question whether the economic analysis of law will ever make an impact on Romanian doctrine in the foreseeable future, my answer is moderately optimistic. The reason it might have an impact lies, in my opinion, on the external influences of the European Union, induced either through French or through German doctrinal prestige. One can only hope that the economic analysis of law leaves the niche of the secured interests and financial operations and becomes a meaningful tool in legal reform in our country. Predictability and efficiency are badly needed in our legal system, and hence academics and practitioners alike shoulder the responsibility to adapt these conceptual tools to foster economic development, without - of course - giving up the traditional approach to the law as a vehicle for justice and fairness. If the economists can make their voices count (overwhelmingly so, of late), so should jurists.

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