

The Economic Roles of Law

- Laws do not play important roles in economic activities in some circumstances
 - Traditional economy
 - Relational transactions (*guanxi*, or connection) in modern economy
- The economic advantages of laws: reducing transaction costs through
 - Transparency
 - Predictability
 - Uniformity

The Economic Roles of Law

- But laws are important in modern economies
 - Laws to constrain economic agents' behavior in dealing with each other (to prevent private expropriation)
 - Laws to constrain government behavior and to protect private interests (to prevent public expropriation)
- Good capitalism vs. bad capitalism
 - The government is a third party enforcing contracts and laws
 - The government does not encroach private property
- Government needs neither too strong nor too weak (Weingast dilemma)

Conceptual Clarifications

- Rule of law vs. rule by law
 - In the former, all agents, including government itself, are under the law
 - In the latter, government uses law to govern, but itself not constrained by laws
- Economic freedom, civil liberty, and political rights
 - Hong Kong is ranked on top of economic freedom index
- Rule of law and democracy

Types of Legal System

- Case Laws vs. Statute Laws
 - Common Law System (Anglo-Saxon)
 - UK, US
 - Continental Law System
 - German
 - Scandinavian
 - French
- Unitary vs. Federal System
 - Federal
 - U.S.
 - Unitary
 - France

Legislating Laws

- Three types of laws in China
 - Civil
 - Economic
 - Administrative
- Laws regulating economic agents' behavior
 - Contract laws
 - Corporate laws and bankruptcy laws
 - Securities laws
 - Consumer safety laws
- Laws regulating government's behavior
 - Administrative Litigation Law
 - Administrative Procedure Act

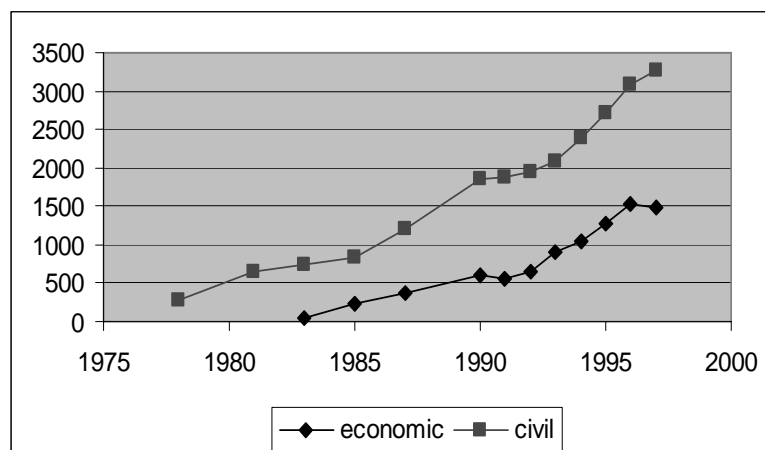
Enforcing Laws

- Institutions for law enforcement
 - Police
 - Prosecutors
 - Courts and judges
 - Lawyers
 - Arbitrators
 - Other informal mechanisms
- Economics of law enforcement
 - Law enforcement is costly
 - Enforcers are human too

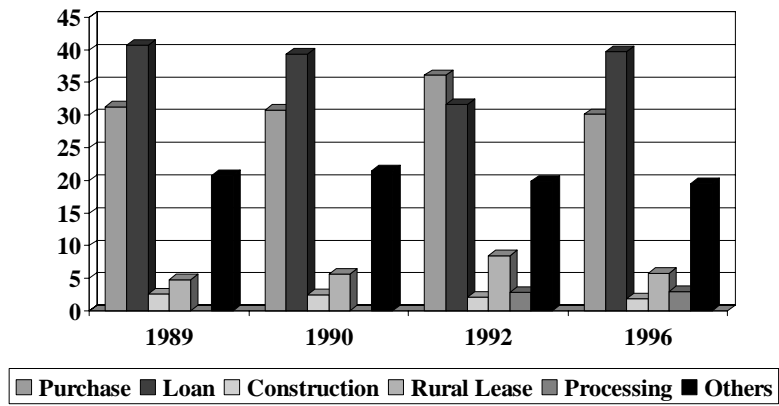
Legal Reform in China

- Legal reform is separated from other political reforms
 - Good: can get legal reform going before democratization
 - Bad: can't have a completely independent judiciary
 - But: huge room exists even without an independent judiciary at the central level
- Legal reform moved fast in the past decade
 - Record speed of enacting laws
 - Qualifications and exams for lawyers, judges, and prosecutors

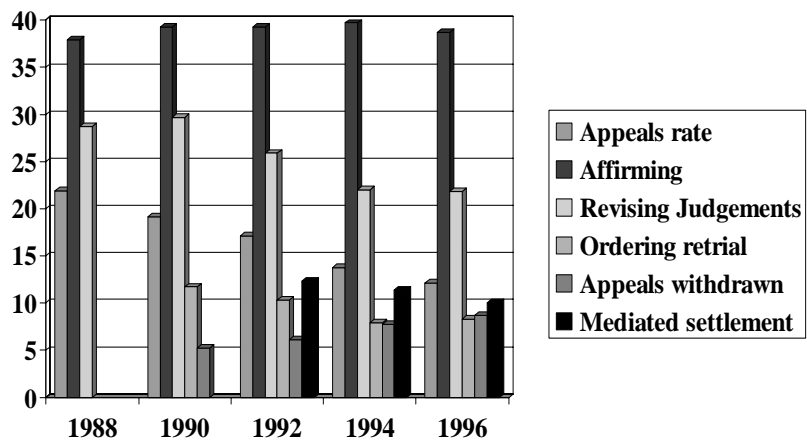
Growth of Litigation: Civil and Economic (accepted cases in the courts of first instance, thousands)



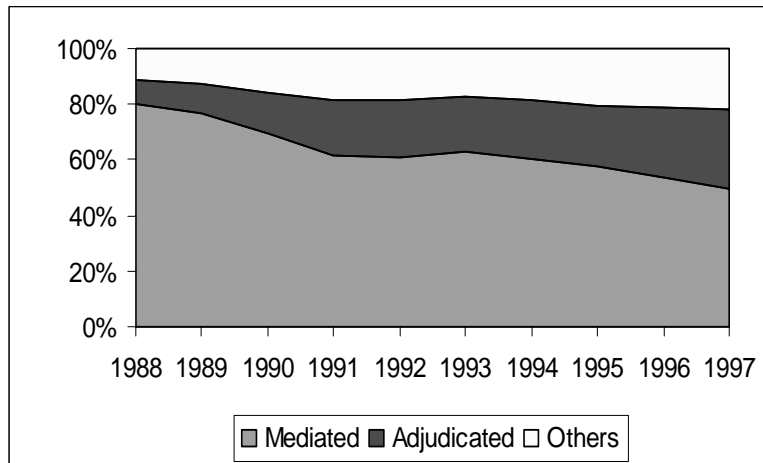
Breakdown of Contract Related Lawsuits (percentage of accepted cases)



Disposition of Appeals in Commercial Disputes (%)



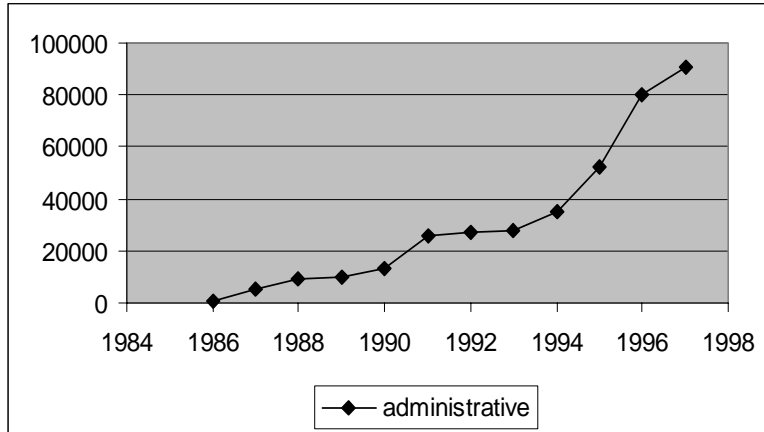
Disposition of Economic Cases (%)



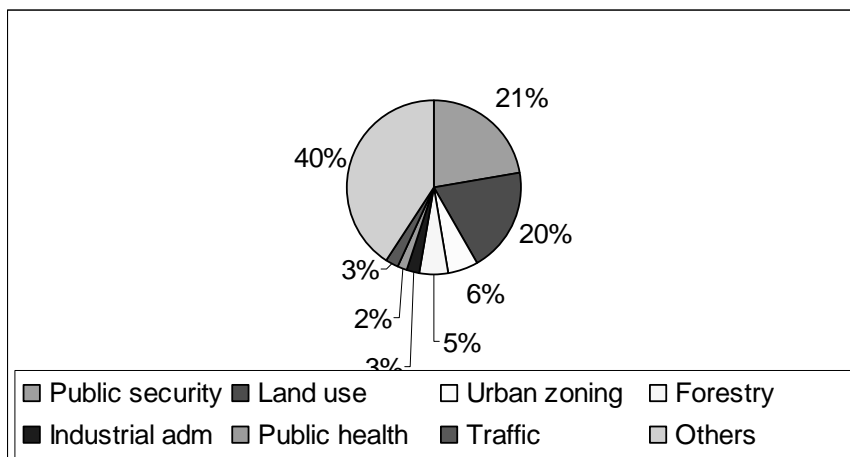
Assessing Administrative Litigation

- The Administrative Litigation Law (passed in April 1989, implemented in October 1990)
 - The legal basis for adjudicating disputes between citizens and the government over administrative decisions
 - Concrete administrative actions vs. general policy
 - Collective suits (class action lawsuits) are allowed
- A case of Peijiawan village, Shaaxi Province (*The Wall Street Journal*, March 25, 1999)
 - 12,000 farmers in 1996 filed a class-action lawsuit against the local government for levying excess fees of \$75,000

Growth of Litigation: Administrative (accepted cases in the courts of first instance)



Administrative Litigation: Composition of Cases (% of cases accepted by the court)



**Administrative Litigation: Disposition of Tried
Cases (%)**

	revoking	upholding	withdrawn	revising	others
1988	11	49	27	5	8
1989	14	42	31	6	7
1990	17	36	36	3	8
1991	19	32	37	2	10
1992	21	28	38	2	11
1993	19	23	41	2	15
1994	19	21	44	1	15
1995	15	17	51	1	16

**Administrative Litigation: Disposition of Major
Categories (1995) (%)**

	revoking	Upholding	withdrawn	revising	others
ALL	15	17	51	1	16
Law enforcement	16	17	50	2	15
Land use	22	29	34	1	14
Urban zoning	15	22	50	0	13
Industrial and commercial administration	17	30	40	0	13

Administrative Litigation: Access to Legal Counsel

	Percentage of plaintiffs with professional counsel	Percentage of defendants with professional counsel
1991	21	36
1992	38	28
1993	35	19
1994	30	17
1995	21	14

Who Sues: Types of Plaintiffs (in a sample, not random)

– SOEs	20%
– Private enterprises	20%
– Peasants	17%
– Workers	11%
– Collective firms	9%
– Unemployed	4%
– Foreign firms	4%
– Professionals	4%
– Cadres	4%
– Collective suits	3%
– Others	4%

Judiciary Local Protectionism

- Local courts protect the interests of local business in disputes
 - Home court advantage
- Why is this a serious problem in China?
 - Local government has strong commercial interests (through taxes, employment, and direct ownership rights) in local business
 - The jurisdiction of the court system coincides with administrative jurisdiction
- Temporary solutions
 - All cases relating to foreign business will be handled by provincial courts, not lower courts (February 2002)
- Long term solution
 - Cross province circuit courts (look at the U.S. case)

The Case of the U.S.

- The Commerce Clause in the U.S. Constitution
 - Article I, Section 8—Power of Congress: To regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes
- The two tier legal system: federal and state
 - States have no rights to regulate inter-state commerce
 - Common market in the U.S.
- Famous cases
 - 1824: Gibbons vs. Ogden
 - State of New York granted Fulton and Levingston monopoly rights of operating steam boats on Hudson River, which is between New York and New Jersey
 - 1827: Brown vs. Maryland
 - State of Maryland imposed \$50 fees on out of state goods

Law vs. *Guanxi*

- Informal mechanisms are important in all societies
- *Guanxi*: personal connections
- Laws and *guanxi* can be complementary
 - Using laws are costly and time consuming
 - *Guanxi* may work better under the rule of law

Legal Reform After WTO

- Joining the international track (*jiegui*)
- The rule of the game under WTO is Rule of Law
- Transparency requirement under WTO
 - Elimination of internal regulations
 - Uniform treatment