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CHAPTER 4

THE RULE OF LAW, ECONOMIC DEVELOPMENT, AND THE DEVELOPMENTAL STATES OF NORTHEAST ASIA

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Rule of Law rhetoric is all around us – in the business press, in the programs and publications of the World Bank, International Monetary Fund (IMF) and Asian Development Bank (ADB), in bilateral development assistance projects, and even in US–China diplomatic dialogue. Notably, however, the Rule of Law is not being touted in these primarily for its traditional political role as a protector of human rights and individual dignity. Rather, the new rhetoric makes the claim that the Rule of Law is a crucial element in economic development, not only in formerly socialist countries ('transition economies') (World Bank, 1996), but in developing capitalist countries as well.[1]

More recently, a separate torrent of Rule of Law language has been unleashed, this time in reaction to the Asian financial crisis. Some of this is serious and well intentioned,[2] while some of it has a distinctly gloating tone.[3] It should be clear, however, that these two claims cannot both be true. If the claim that East and Southeast Asian societies lack the Rule of Law is true, this presents a serious challenge to the first claim, given that these parts of Asia have been the economic development success story of the twentieth century. A compromise position might be to posit that the Rule of Law becomes necessary once a certain level of economic development and complexity has been reached, now the case in a country like South Korea. This position would fit well with the idea being put forth elsewhere that an 'Asian model' was effective for catching-up, but that the model suffers from inherent flaws that make it ineffective for an advanced economy. But even this more nuanced approach, to the extent that it admits a lack of the Rule of Law in, for example, Taiwan of the 1960s and 1970s, presents a clear challenge to claims for the necessity of the Rule of Law for economic development.

This chapter will attempt to evaluate some of these economic claims for the Rule of Law in the context of post-World War II Northeast Asia, defined as Japan, South Korea, and Taiwan. The focus will be on economic governance in these countries during the decades of high economic growth, the 1960s and 1970s, the era that spawned the moniker 'developmental

state.'[4] A necessary starting point for such an exercise is a working understanding of the Rule of Law as a concept, found in the second part of the chapter. The third part moves from a discussion of the Rule of Law to an examination of how the concept is being used in the Rule of Law-economic development literature. The nature of that literature requires that this effort be somewhat impressionistic, but two interrelated concerns are apparent: the Rule of Law as the protection of private property rights, and the Rule of Law as a limit on government discretion.

The fourth part of the chapter explores to what extent the Rule of Law in these two senses functioned in the 'developmental states' of Northeast Asia. The conclusion is that the Rule of Law as a system of fairly stable property rights and contractual relations functioned well, but that this was not necessarily a result of the Rule of Law in any full sense. Other functions of the Rule of Law, for example as a curb on government discretion in economic governance, were just as clearly not met, however. Out of the empirical investigation of the fourth part, the fifth part argues that there are serious problems with the present Rule of Law-economic development rhetoric, problems that are related to the fact that the rhetoric doesn't reconcile easily with the Northeast Asian experience. The chapter concludes with a call for further use of empirical knowledge of Northeast Asia to test universalist theories in the social sciences generally, not only in the relationship between law and economic development.

AN INITIAL PROBLEM: WHAT IS THE RULE OF LAW?

The first task in this exercise must be a definition of the Rule of Law. Below I discuss two related, but somewhat distinct, ways of thinking about the Rule of Law, the first more traditionally jurisprudential, the second more in the socio-economic tradition.

To many jurists and philosophers of law, the term 'Rule of Law' brings to mind an array of particular yet related concerns about how a just legal system should operate.[5] These concerns with the administration of justice mark this approach as more procedural than substantive, and most would agree that these are aspirations, and that failures to meet the aspirations are found in all legal systems.[6] In this tradition, therefore, to say that a society is characterized by the Rule of Law could only mean a high number of these goals being met a high percentage of the time, and it is rare to find jurists using the term as a benchmark for comparing different legal systems.[7]

An alternative way of thinking about the Rule of Law is as describing the condition of a society governed by a complete and functioning legal infrastructure, governing relations both among private actors, and between

private actors and public authorities. The independent judge as enforcer of the rules and of privately bargained out contracts is important in this way of thinking about the Rule of Law, but the phenomenon of judging itself, and the challenges that the act of judging pose for the Rule of Law, is not the focus. It is in this sense, which could be described as heavily positivist formalism,[8] that the term is being used in the economic development literature.[9]

The relationship between these two paradigms is complex. Legal scholars tend to approach the Rule of Law in the first mode, testing the extent to which the various aspirations of the model are met by examining judicial decisions, often focusing on difficult cases. This approach highlights judicial discretion, judicial law making, and weaknesses in the system of rules, even if many who write in this tradition would accept that rules are often relatively clear, and often do shape social action in predictable, understandable ways. The jurisprudential approach tends not to address the broad issues of economic performance that are the focus of the Rule of Law-economic development literature.

Thinking about the Rule of Law in the second mode, as shorthand for a functioning legal infrastructure, requires one to proceed as if the aspirations of the first model were met without serious qualification in certain 'Rule of Law' societies. The goal is to reduce the Rule of Law to a fact about an economy, similar to its literacy rate, or the level of union membership in its workforce, thus facilitating a certain kind theorizing about the relationship between the system of courts and rules, and socio-economic behaviour (Knack and Keefer, 1995).

In spite of obvious conflict between the two approaches, the second approach appears able to exist alongside, but also in isolation from, the first for at least two reasons. First, its practitioners tend to be economists, political scientists, or historians, not jurists.[10] Thus they tend to lack formal training in law, at least not the experience of actually reading lots of cases deciding economic disputes in which the applicable rules, defining the rights of the parties, were surprisingly unclear or debatable. Not being jurists, they also have not had the additional education of working as a judicial clerk or as an attorney, situations which teach that the administration of a legal system is much more than the application of rules to facts, and that contracts are not always clear, written memorials documenting the results of market bargaining over property rights. Second, if those who approach the Rule of Law as legal infrastructure took the issues raised by the jurisprudential approach too seriously, it could undermine their effort to understand the relationship between the framework of rules and social life, just as ideas of bounded rationality tend to undermine simplistic rational actor models of politics and economics.[11]

SUBSTANTIVE CONCERNS OF THE RULE OF LAW-ECONOMIC DEVELOPMENT RHETORIC[12]

As an alternative to focusing on definitions, which might reflect an unrealistic concern with conceptual clarity, a more productive approach may be to identify the substantive concerns underlying the Rule of Law–economic development literature. The rhetoric generally revolves around two core themes: defining and enforcing private property rights, and reducing bureaucratic discretion in economic governance.[13] The 'property rights–Rule of Law' branch can be again divided into at least two separate strands. A more theoretical and abstract strand focuses on property rights for their role in the functioning of a market economy (World Bank, 1996:44-65), while a second strand focuses on the effective enforcement of statutory law creating and protecting more particular economic rights, such as statutes on intellectual property or competition law. The second main branch of the Rule of Law-economic development rhetoric addresses itself to limiting bureaucratic discretion, to binding official action within the strictures of the law and the machinery of justice. In this sense it tends to overlap with contemporaneous discussions of transparency, anti-corruption, and 'good governance.'

Private Property Rights and Economic Development

Rule of Law rhetoric focusing on the creation and protection of property rights can be seen as guided by two different clusters of themes and concerns. The first addresses itself to property rights as the basic object of market activity. This literature is grounded on the truism that market exchange implies at least some basic right of control over the object to be exchanged. The literature then addresses itself to the 'security' of these property rights as a precursor to economic success or failure. The second area where Rule of Law rhetoric arises in connection with property rights focuses on the effective enforcement of statutory regimes creating particular rights, or enforcing certain market conditions.

The Rule of Law as the Creator of Property Rights, Building Block of Markets

The primary focus of this branch is on positive law enshrining private property rights, courts to enforce those rights according to the pre-established law, and state organs ready to enforce the rulings of the courts.[14] Enforcement *vis-à-vis* other private actors, which includes both the enforcement of contracts and the enforcement of criminal law,[15] is seen as necessary for the free contractual exchange of property rights, the basic activity in a market economy.[16] Enforcement *vis-à-vis* the state is seen as

necessary to prevent arbitrary state interference with private property.[17] In the words of the World Bank, 'markets cannot develop very far without effective property rights. Those rights can only work with three preconditions: first, protection from theft, violence, and other predatory acts; second, protection from arbitrary actions, ranging from ad-hoc regulation and taxes to outright corruption that disrupts business activity; and third, a fair and predictable judicial system (World Bank, News Rel: No 97/1380/S).'

Writings in this more abstract branch of the property rights-Rule of Law rhetoric, in their emphasis on legally created and enforced property rights as part of the structure of a market economy, reflect the influence of 'new institutionalism' in economics and political economy, and more specifically, the claims of Douglass North (1990:139), Mancur Olson (1993:567, 574) and others concerning the importance of property rights in the economic development of the West.[18] Although North's extremely broad definition of an 'institution' seems clearly drawn from Weber's sociological approach, or perhaps from Karl Popper (1976:103-4) (institutions include 'any form of constraint that human beings devise to shape human interaction,' (North, 1990:4) including formal legal rules as well as social norms), North still sees the institutional structure in essentially positivist-formalist terms, demonstrating his affiliation with the 'legal infrastructure' approach to the Rule of Law. For North, institutions are 'the framework within which human interaction takes place. ... perfectly analogous to the rules of the game in a competitive team sport' (North, 1990:4). These rules determine the cost and incentive structures of societies, and can be more or less congenial toward productive behaviour.[19]

Of particular interest to those with East Asian expertise is how easily government with any degree of autonomy from the private sphere, a hallmark of the 'developmental state,' becomes the villain in this story in terms of economic development. Government unresponsiveness to private interests (the 'transaction costs of the political marketplace') explains for North, in large part, the inability of a society to move to a more efficient property rights regime.[20] Taking seriously the prescriptive implications of this view would encourage even well-intentioned international bureaucrats to suppress reservations about intervening in domestic political affairs, as inefficient property rights are now seen as the result of unjustified transaction costs in the local political system, ripe for progressive reform. The shape and content of a country's entire domestic legal regime can thus be reduced from sovereign political to purely technocratic economic matters.[21] It seems clear from reading the literature that the speculations of North, Olson, and others have provided important theoretical justification for the drastic expansion of the IMF's involvement in domestic legal and

political affairs that is finally being brought to mainstream attention by the crisis in East Asia.[22]

The Rule of Law as Effective Enforcement of Statutory Regimes

The second strand of the 'property rights' branch of the Rule of Law-economic development literature attempts to connect economic development to the aggressive enforcement of legal regimes that protect rights and interests beyond those normally seen as necessary to constitute a market economy.[23] These claims are probably most prevalent in the areas of intellectual property rights (IPR) and trade, but are heard often now in connection with competition law.

Enforcement of a statutory regime in Rule of Law terms is enforcement on non-political, purely formal legal grounds, uninfluenced by substantive political concerns and without instrumental aims. For example, a Rule of Law IPR regime would mean, in these terms, not only positive law creating rights, but also a court system that is practically available to private litigants, that reaches its decisions on the basis of the law alone, uninfluenced by non-legal objectives, and that has effective enforcement powers.[24] Legal assistance programs thus often emphasize the training of the legal functionaries, the examiners, judges, and prosecutors, of developing countries,[25] presumably in the hope that they will begin to aggressively enforce existing IPR regimes in a Rule of Law manner, i.e., without reference to extraneous substantive considerations such as whether the law is being invoked by a foreign entity against a domestic manufacturer trying to localize an expensive, or perhaps unavailable, technology.

A good example from the area of international trade is the way in which the US State Department invokes the Rule of Law to suggest why joining the WTO will benefit China:

> To meet WTO requirements, China must make laws public, require judicial review of all trade actions, apply all trade laws uniformly, and submit to WTO dispute settlement to ensure compliance with WTO rules. *All of these measures will enhance the rule of law* and the application of international norms in China's trade regime, to the benefit of China and the United States. *The rule of law in trade has spillover benefits to the rule of law elsewhere.*[26]

In the area of competition law we find a similar set of concerns: effective enforcement means not only an appropriate statutory framework, but also an enforcement authority that is adequately staffed, adequately insulated from political and private pressures, and that seeks to actively enforce a non-cartelized, non-monopolized market economy (World Bank, 1996:92-3).

The Rule of Law as invoked here tends to mean, in historical terms, the active enforcement, primarily for the benefit of foreigners, of positive law that countries have adopted in order to comply with international norms, or to benefit from participation in the international economic system, but which has been implemented in ways which are not seen by the international community as appropriate.

Limiting Discretion in Economic Governance

The second main branch of the Rule of Law-economic development rhetoric focuses on using law and the courts to legalize government processes and strictly limit official discretion, often put in terms of increasing the transparency or accountability of governance.[27] A good example of this vision of the Rule of Law can be found in the World Bank's *World Development Report 1997: The State in a Changing World.* In the Report, the Bank puts forth a two-prong strategy for defining the proper role of the state in a developing economy: i) matching the state's role to its capabilities, and ii) increasing state capability by reinvigorating public institutions (World Bank, 1997:3). Not surprisingly, however, 'reinvigorating public institutions' involves a heavy dose of 'new institutionalist' Rule of Law thinking, which itself draws heavily on 'public/rational choice' analyses of politics.[28] The report emphasizes first and foremost the need to bind state actors within a system of 'effective rules and restraints,' before moving on to list other approaches to improving the performance of state institutions (World Bank, 1997:3, 7-11).

Limiting official discretion is not always put forth as a goal in itself; rather, what is usually put forth is one of the assumed benefits of limiting official discretion, such as reducing opportunities for official corruption,[29] or increasing the predictability of the regulatory environment by preventing arbitrary state action, thus encouraging private investment activity. In this way, limiting official discretion tends to become synonymous with 'good governance,' and it is here that the IMF in particular seems to have found justification for the 'mission creep' that has brought it into the Rule of Law business. Although there is no necessary connection between the desire to bring bureaucratic discretion within the Rule of Law and a deregulatory substantive agenda, cynicism about the ability of an activist government to refrain from rent-seeking seems to result in a blending of the two, so that subjecting government discretion to the Rule of Law is presented as requiring substantive deregulation.[30]

Arguments for the importance of transparency in governance are most persuasive in discussions of foreign investment climates,[31] while they appear less persuasive than the 'property rights-Rule of Law' rhetoric with regard to the purely domestic functioning of an economy. After all, what is opaque

to outsiders may be perfectly transparent to national economic actors, particularly large ones.[32] Perhaps reflecting this issue of perspective, transparency from the outsider's perspective is raised to an economic necessity by the claim that it is a key to a country's attractiveness to foreign investors, who, in turn, are presented as being necessary for economic development.

WHAT THE NORTHEAST ASIAN 'DEVELOPMENTAL STATES' SUGGEST ABOUT THE RULE OF LAW AND ECONOMIC DEVELOPMENT

Following this rough outline of the major themes of the Rule of Law-economic development literature, we now turn to an evaluation of these claims in light of Northeast Asia's experience in economic development post-1945.

Private Property Rights and Effective Enforcement of Statutory Regimes

In the third part above, the concerns addressed by the Rule of Law-economic development literature were first divided into two branches, one concerned with property rights, the other concerned with limiting government discretion in economic governance. The property rights branch was then divided into two strands, one focusing on property rights as the basis for market behaviour, the other on the effective enforcement of particular statutory regimes.

Creation and Protection of Private Property Rights

This strand of the 'property rights-Rule of Law' rhetoric emphasizes the role of law in creating and protecting the private property rights owned and traded by private actors in the market. Independent courts are a key component of this vision of the Rule of Law, as protectors of the sanctity of contract, and as a check on arbitrary interference by the state with private property.

At first glance, Northeast Asian economic development seems to support the connection between economic development and this 'property rights' version of the Rule of Law, given that Japan, South Korea, and Taiwan were all market economies based largely on private ownership, though with some important qualifications, such as state ownership of banks in both South Korea and Taiwan, and a very large state enterprise sector in Taiwan. The importance of the particular rights created by the positive law, and the necessity of active, independent courts for the protection and functioning of these rights, is less well supported, however.

First, at least some forms of private property were long present in Northeast Asian societies prior to the importation of Western law, as were sophisticated trading systems (Scogin, 1990:1325; Henderson, 1968:203), yet traditional Northeast Asian formal law did not concern itself primarily with the creation and enforcement of private property rights. When Western rights-oriented law was adopted in Northeast Asia, it accompanied other modern economic institutions such as modern banking and accounting practices, modern corporate forms, modern manufacturing technology, etc., which might have functioned in Northeast Asia even without the same legal infrastructure with which they grew up in the West. The existence of traditional socio-cultural norms and practices favourable to private property and market behaviour at least raises the possibility that the more complex legal relationships of a modern economy were effectively instituted and have functioned in Northeast Asia without being as dependent upon the legal system as the Rule of Law-economic development literature would posit as necessary, in particular, with comparatively less enforcement by the judicial system. While some clearly understate the role law has played in the economic systems of Northeast Asia,[33] the experience there does at least suggest that the creation of clear positive law as well as highly user-friendly and powerful courts may not be strictly necessary in societies with an existing social/cultural consensus favouring private property and trade.

Second, it is no coincidence that Northeast Asian societies have been the inspiration for much speculation about socio-cultural factors as supplements to, or functional equivalents to, judicial enforcement of contracts.[34] Although the literature on 'relational contracting,' 'social capital,' and Chinese business networks tends to praise the pervasiveness of these extra-legal sources of stability in exchange relations, suggesting a gain from legal informality (Winn, 1994:193; Upham, 1994:233), it is interesting to remember here Franz Neumann's argument that the formal Rule of Law may have been demanded by economic actors in the 'competitive capitalism' of the nineteenth century West, as Weber argued, but that 'monopoly' capitalists did not need formal legality to protect their rights in the market, and actually benefited from greater informality.[35] Thus, against all the potentially positive aspects of relational contracting and legal informality in Northeast Asia we should counterpoise the potentially negative aspects of private ordering unconstrained by law. We should also take this into account when trying to understand to what extent demand for the Rule of Law at even this basic level existed in the 'developmental states.'[36] This is not simply an interesting academic question, however. As the international economic institutions try to compel both mass privatization/deregulation and the Rule of Law in countries like Russia and the People's Republic of China (China), we should keep in mind that the

first objective, especially if it takes place too quickly, may result in societies dominated by private economic actors not only indifferent, but hostile to, the Rule of Law (Liu and Link, 1998:19-23).

Northeast Asian societies are also cited for their low rates of civil litigation, and even if these claims are overstated, they suggest caution in making strong claims for the necessity of easily accessible and effective judicial dispute settlement for a functioning market economy.[37] Low litigation rates in Northeast Asia arguably have more to do with material disincentives such as legal fee structures and inconvenient court procedures and fees than with cultural aversions to judicial conflict resolution, though arguably these material disincentives are themselves the result of political/cultural factors shaping the implementation of the imported legal institutions. In any case, however, low levels of litigation suggest either that the formal legal norms are so clear and well integrated into these societies that they are law-governed without much resort to the courts, ironic considering the usual thinking that the assimilation of Western law has been difficult in Northeast Asia, or that the particular form of the positive law and the threat of court enforcement has not been of primary importance in market behaviour there. The relatively low incidence of civil litigation in Northeast Asia should at least caution against simplistic approaches to understanding the complex relationship between courts, rules, and market behaviour.

Turning to the clarity and judicial enforcement of contracts, a theme often emphasized in the economic development literature that deals with the Rule of Law, one would expect the greatest clarity of rights in fairly simple transactions, where it is plausible that the language of the contract and the relevant law would be sufficiently clear so that a judge could simply enforce bargained-for rights. This, however, is precisely the level at which so much is made of the importance of relationships in Northeast Asia, and the reluctance to litigate contract disputes. As the level of complexity of exchange increases, a paradox arises. According to North's evolutionary model, which seems to be accepted by the World Bank, social norms or other non-legal institutions can be relied upon to enforce simple exchange contracts, but increasing complexity of exchange will not be possible without reliable, authoritative judicial enforcement.[38] This certainly seems right, but on the other hand, as the complexity of the contract to be enforced increases, it seems to become increasingly difficult for a judge to perform his/her Rule of Law role of simply sorting out bargained-for rights based on the existing infrastructure of rules.

At least according to the perceived wisdom, Northeast Asian economic actors have not dealt with increasing transactional complexity by attempting to draft contracts that cover all possible contingencies, as we tend to do in

the US, and which would thus assist a court in parsing out rights in a complex transaction. The amount of even relatively complex, long-term contracting done on the basis of fairly simple written contracts suggests that the demand for full clarity of rights, especially through judicial enforcement, has been lower in Northeast Asia than would seem necessary from reading the Rule of Law-economic development literature.

In the context of present-day East Asia, the rhetoric of clear property rights is often employed with regard to the transformation of Chinese State-owned enterprises (SOEs), and the necessity of creating stable private property interests in these entities so that the dysfunctional incentives of current managers can be replaced by the appropriate incentives of private shareholders (World Bank, News Rel: No 98/1425). However, this emphasis on the necessity of creating clear private property rights in Chinese SOEs, based as it seems to be on prevailing US corporate governance theory, is also called into question by the Northeast Asian experience in corporate governance. Few would argue that Japanese, South Korean, or Taiwanese corporate managers have been effectively disciplined by shareholders in the way that liberal corporate governance theory calls for. They were not disciplined by market forces created by widely dispersed shareholders buying and selling shares in highly liquid markets, nor by 'markets for corporate control,' nor by shareholder derivative suits, despite the existence of provisions for such suits in the corporate laws.[39] This has long been discussed in the comparative corporate governance literature, where the focus has been on the comparative effectiveness of Japanese corporate governance, particularly the *keiretsu* structure of stable cross-shareholding arrangements and 'main bank' monitoring of management. To the extent, therefore, that the property rights-Rule of Law rhetoric makes strong claims for the necessity of corporate governance arrangements based on current US thinking, the history of corporate governance in East Asia suggests that such claims are overdrawn.[40] This call for caution is supported by the candid admission of one writer for the OECD that, 'the interrelation of corporate governance and corporate performance ... is a subject which is in its infancy and it is unquestionably premature to base policy decisions on the evidence which is available to date' (Mayer, OECD Working Paper: No 164).

One also encounters property rights-Rule of Law language in discussions of foreign investment climates, claiming that foreign investment is conditional upon the Rule of Law.[41] But the Northeast Asian experience shows that what passes for the Rule of Law in this context should be understood as essentially a political commitment to keep order and to not expropriate foreign investments, and should not be confused with a Rule of Law in any deeper sense.[42] This simple commitment probably is necessary for economic development that depends to any degree on private initiative,

but should not be confused even with a Rule of Law limited to strict judicial protection of private property rights.[43] In China, for example, one finds enormous foreign and domestic investment in the shadow of a political and quasi-legal commitment to protect private property in the constitution and various statements in specific laws and regulations, but no sense that at this point this commitment is met through a domestic Rule of Law in the sense that foreign (or domestic) investors could count on effective judicial protection of their property interests. There are grave difficulties with the enforcement of purely domestic civil judgments against private parties in China,[44] to say nothing of judgments against the government. Whether or not China would have more foreign investment if it had a more developed legal system cannot be proven, but at least over the last fifteen years foreign investment and domestic economic activity have proceeded in the presence of a political commitment in favour of development and to protect foreign-invested property, but in the absence of even a 'property rights' Rule of Law.[45]

Portfolio investment by foreign investors is also often said to depend upon clear, enforceable shareholder rights, although this claim too seems problematic in light of the Northeast Asian experience. Foreign portfolio investors have invested in Northeast Asian stock markets with little interest in exercising their rights as shareholders, primarily to gain exposure to fast growing economies and to diversify their portfolios. The 'developmental state' model forced this approach by limiting foreign portfolio investment, so it is impossible to say how investors would have behaved in the absence of such limits. Clearly the 'developmental states' developed rapidly with limited foreign portfolio investment, which served political objectives of industrial and technological autonomy and self-sufficiency, and relative insulation from international market forces.

Finally, the current financial crisis has demonstrated how willing banks have been to lend to private borrowers around Asia, a form of foreign investment, despite the absence of legal regimes requiring a great deal of transparency, or providing effective creditor protection in cases of bankruptcy.[46] The Asian Development Bank would have us believe that, '[C]ommercial lenders ...will not come to a country unless it can offer an attractive ... lending climate, an important component of which is an effective and protective legal and regulatory framework (Asian Development Bank, 1997), but such a broad claim risks over-emphasizing legality at the expense of a realistic assessment of business interests. The current crisis shows that we would all have been better off had lending banks insisted on transparency and clearly enforceable rights in their Asian lending operations, but the crisis itself puts lie to the claim that lenders' own interests lead them to demand these elements of the Rule of Law.[47]

Effective Enforcement of Statutory Regimes

Rule of Law rhetoric is also commonly invoked in connection with attempts to encourage developing countries to enforce certain statutory regimes more aggressively, particularly IPR and competition law regimes. For example, the US Government's trade strategy now includes a drastically increased emphasis on effective enforcement, and often puts this emphasis in Rule of Law terms. The aggressiveness of this new emphasis on enforcement in developing countries suggests that important actors now recognize that such legal regimes were systematically and intentionally 'under enforced' in developing Northeast Asia. For example, the agenda of the United States Trade Representative (USTR) in China seems to be an implicit acknowledgment that IPR enforcement in other Northeast Asian countries was intentionally weak, as well as a commitment to preventing China from following the same path.[48]

Given this tacit acknowledgment, and the fact that the other Northeast Asian countries are now technologically very advanced, it seems absurd to argue that effective IPR protection is intrinsically necessary to economic development, though of course it can be made necessary by threat of technology boycotts, or by linking IPR protection with other trade issues. It is often argued that the incentive structure for local intellectual property (IP) creators also depends upon effective IPR enforcement, but at what point the benefits of protecting locally-produced IP outweigh the costs of protecting foreign IP obviously varies from country to country, and with technological change, and would seem impossible to calculate absent drastic simplifying assumptions.

A relatively new agenda for international Rule of Law advocacy is in competition law. Here again, the notorious under-enforcement of competition law and monopoly regulation in Japan, South Korea, and Taiwan provides reason for scepticism about claims that active competition law enforcement is in some way necessary for economic development. Part of the 'developmental state' model has included the creation of business groups large enough to compete internationally in industries where economies of scale are crucial, as well as the *de facto* and at times *de jure* cartelization of many industries. Both of these features of the 'developmental state' would be undermined by fully independent, enforcement-oriented competition law authorities, which perhaps best explains why competition law has played such a minor role in shaping the economies of Japan, South Korea, and Taiwan. In the words of Japan scholar Christopher Heath, '[w]ithin the framework of an economic policy that clearly puts Japanese interests first, an independent antitrust agency that upholds the rule of law and thereby prohibits cartels simply does not fit in.' (Heath, 1997:433).

LIMITING GOVERNMENT DISCRETION IN ECONOMIC GOVERNANCE

The other main branch of Rule of Law-economic development rhetoric speaks in terms of making the government as well as the citizen subject to the law, though it tends to focus on the activities of lower level state functionaries, rather than insisting on democratic participation in the law making process. This section of the chapter will examine some areas of bureaucratic governance integral to industrial policy in the 'developmental states' to see whether, or to what extent, a Rule of Law functioned.[49]

Credit Allocation

One of the central elements of the 'developmental state' model has been government involvement in the allocation of credit, beyond simply providing the framework for financial market activities. This has been accomplished through direct government ownership of the banks, as in South Korea (Jung-En, 1991) or Taiwan (Jia-Don and Yang, 1994:193), or through less direct means in Japan.[50] Governments have sometimes 'replaced' markets, as where all lending for a particular project or industry has come from the government or at government direction, and sometimes governments have 'guided' markets by providing some funding, and thus signalling that private lending to that company or industry was favoured and would be relatively secure.

Although government involvement in credit allocation raises interesting questions for political science[51] and economics,[52] for purposes of an inquiry into the Rule of Law the important questions concern neither the existence nor the effectiveness of policy lending, but rather the means by which it was and is carried out. Once government involves itself directly in the allocation of credit its actions can be analysed in Rule of Law terms. Assuming that the government is pursuing substantive objectives in allocating credit, some way to decide between different applicants for credit is necessary. Inquiry into the Rule of Law would then centre on how allocation decisions are made, and how the discretion retained by the relevant government actors is contained and structured. Assuming that the government actors act under some general statutory authority, do they themselves act to cabin their authority by publishing binding rules or even non-binding policy statements governing how lending decisions will be made? Are criteria publicly available which, if met, would entitle an applicant to receive policy loans, in some sense as a matter of right? Is judicial review available to enforce transparency in policy loan administration or to try to ensure that decisions are made based on legitimate rather than on irrelevant or corrupt grounds?

These questions are crucial to any exploration of the Rule of Law in this crucial facet of the 'developmental state.' Like any similar regulatory

program, policy lending will involve a good deal of discretion on the part of the implementing officials. But this discretion can be limited and shaped by various means to meet some of the objectives of the Rule of Law, or this discretion can be exercised within a 'black box,' so that only insiders can guess at the exact constellation of considerations, legitimate or otherwise, that lead to a particular decision. The freeze that South Korea's Kim Young-sam government imposed on lending by formally private banks to the Hyundai Group, sadly reminiscent of the destruction of the *Kukje* Group by the Chun Doo Hwan government, suggests that at least in the South Korean context executive branch influence over lending policy is little constrained by Rule of Law considerations.[53] There was reportedly concern that current President Kim Dae-Jung would attempt similar reprisals against the Samsung group because of personal antagonism against Chairman Lee Kun-hee (Lee, 1998), and while international observers generally praise the South Korean government's 'Big Deal' policy, under which *chaebol* are exchanging and merging subsidiaries in order to rationalize the Korean industrial structure, serious concerns are being raised as to the legality of the methods the government is employing to obtain *chaebol* co-operation. In Japan, as well, the ability of the Ministry of Finance to influence the Bank of Japan, which in turn was able to influence private bank lending decisions, has been described as a particularly lawless phenomenon (Mabuchi, 1993; 1997).

Screening of Foreign Investment

The Rule of Law has traditionally been seen as an attribute of national governance, between a government and its citizens, or it is invoked in the international arena, to describe a situation where relations between states are governed by international law, rather than simply by force. What is not found in these two traditional contexts, but what seems to be implicit in the Rule of Law-economic development conception, is that a sort of administrative, or procedural, Rule of Law should govern relations between sovereign governments and foreign economic actors.

But should a government be criticized for not upholding the Rule of Law because it retains discretion to screen foreign investment based on non-Rule of Law concerns, such as foreign dominance of its domestic industry, or the amount or appropriateness of technology being transferred by foreign investors? Although Northeast Asia generally escapes attacks on the 'New International Economic Order' (NIEO) movement of the 1970s, which sought to legitimate screening of foreign investment,[54] such discretion was rampant in the heyday of the 'developmental states,' which did not recognize 'rights of establishment,' 'national treatment' or MFN obligations with regard to foreign investment applications, and where foreign investors

generally went to the governments, rather than to the courts, to try to influence exercises of bureaucratic discretion in the foreign investment approval process.[55]

This raises again the conflict between Rule of Law-economic development rhetoric, and the complex reality of foreign investment decisions.[56] It is often stressed that foreign investors demand certain Rule of Law attributes from the legal systems of the countries in which they invest, yet foreign investors might fare worse under a Rule of Law system that forced respect for lawful exercises of bureaucratic discretion, unless at the same time they can have the scope within which such discretion can operate permanently narrowed. This is in fact the tack that is being taken internationally, in the various initiatives to create a multilateral regime to discipline national foreign investment regimes[57]

Tax Administration

A third area of economic governance that raises Rule of Law concerns is tax administration. Given the impossibility of auditing all taxpayers, tax officials in perhaps any system will be left with discretion to decide which taxpayers will be audited, a discretion similar to prosecutorial discretion. Rule of Law concerns could be met by a purely random selection system, by a system where all taxpayers meeting certain pre-established criteria would be audited, or by some sort of 'probable cause' requirement to preclude audits based solely on criteria unrelated to the likelihood of improper underpayment. What the Rule of Law would seem to exclude would be a decision to audit based upon considerations unrelated to revenue collection, such as whether the taxpayer had followed 'administrative guidance' in some formally unrelated matter.

Although evidence is difficult to find, it is often alleged that tax audits have been used as a disciplinary tool by the 'developmental state' to enforce administrative guidance that was unenforceable through legal means.[58] This flies in the face of the Rule of Law, but it is not entirely clear that such behaviour by the government would undermine the predictability objective of the Rule of Law, considered necessary for economic activity.

This raises again the issue of administrative guidance and the Rule of Law, and highlights the fact that the problem with administrative guidance from a Rule of Law perspective is not its existence, but its enforcement. If, as is often alleged, ministries are able to coerce compliance with administrative guidance in one field by threatening retaliatory measures in other regulatory fields, such as taxation, policy lending, access to foreign exchange, or business licensing,[59] such retaliatory measures would be motivated by considerations unrelated to that other field, and thus arbitrary from a Rule of Law perspective.[60] Aggressive judicial review would seem to

be the only way to stamp out such cross-jurisdiction, or cross-issue, enforcement, even if appealing for relief through political channels is effective in individual cases.

To conclude this part, it seems that from the role of courts, to the enforcement of statutory regimes, to government discretion in economic governance, the experiences of Japan, South Korea, and Taiwan in the 'developmental state' era at least raise questions about easy connections between the Rule of Law and successful economic development.

ENGAGING THE RULE OF LAW-ECONOMIC DEVELOPMENT RHETORIC

If it is so difficult to reconcile the Rule of Law-economic development rhetoric with the actual development experience of Northeast Asia, it makes sense to examine the usefulness of that rhetoric with regard to today's developing economies. The following passages will examine first what it means to try to reduce the Rule of Law to a social science variable. The question will then be raised whether the Rule of Law-economic development approach is likely to help, or hinder, development of a normatively attractive Rule of Law in any society.

Problems with the Rule of Law as a Social Science Variable

Whether one takes a jurisprudential or a legal infrastructure approach to the Rule of Law, caution is called for when trying to reduce the concept to a variable for social science theorizing. Looking first at the jurisprudential approach, while most in the Anglo-American tradition could, if pressed, agree on a core set of concepts required in any definition of the Rule of Law, there is ample room for disagreement over the inclusion of additional concepts within the core, and over the interpretation and carrying out in practice of the principles in the core.[61] Second, the specific principles that are included within the definition, whatever they are, are in the nature of goals toward which it is thought a legal system should aspire. Thus, even if one proceeds on the assumption that the goals are in fact desired, the utility of an over-arching concept such as the Rule of Law can have only relative significance when all the elements of the umbrella concept are in fact aspirations rather than concrete achievements of any existing system. A final problem arises once one treats the elements as aspirational, however, because even if one favours the Rule of Law, few who think seriously about the relationship between formal rules and substantive justice, however defined, are likely to favour complete fulfilment of all of its elements all of the time.[62] Perhaps reflecting this seemingly perpetual problem, actual legal

systems since Aristotle have arguably violated a strict Rule of Law by allowing judges discretion to pursue substantive justice when strict rule application would result in injustice (Vinogradoff, 1914:208-33).

Use of the Rule of Law in the second sense, as describing a comprehensive functioning infrastructure of rules, rights, and courts to enforce them, runs into problems of its own, however. As a factual matter, modern legal systems have moved from a reliance on rules to a reliance on more indeterminate principles and standards in many fields of law. Nearly sixty years ago, Roscoe Pound wrote:

> If we look only at the precept element [of law], that element includes principles and conceptions and standards as well as rules, and the technique of developing and applying rules, principles, conceptions, and standards, and the received ideals in the light of which they are developed and applied, are as much authoritative and as much part of the law, using law to mean the body of authoritative grounds of and guides to determination, as the rules themselves.[63]

Even Justice Scalia (1989), in a recent article entitled, 'The Rule of Law as a Law of Rules', concedes that 'legal determinations that do not reflect a general rule can [not] be entirely avoided. We will have totality of the circumstances tests and balancing modes of analysis with us forever... All I urge is that those modes of analysis be avoided where possible; that the *Rule* of Law, the law of *rules*, be extended as far as the nature of the question allows (Scalia, 1989:1186-7).' Furthermore, an independent judiciary, seen as necessary in this approach to prevent arbitrary state interference with private property rights, ensures a certain level of unpredictability in judicial decision-making. Judges insulated from political and economic pressures are arguably constrained by the positive law, by their professional training and culture, and perhaps in other ways, but they are not automatons.[64] Thus the idea that one could accurately model the combined economic effects of statutory change and a truly independent judiciary contradicts itself. Some Rule of Law-economic development literature seeks to minimize this obvious problem by suggesting that these 'independent' judges be trained to apply the law in a market-friendly manner, echoing a tactic employed by property rights advocates in the US.[65] In their admission of judicial discretion and open call for instrumental, results-oriented judging, however, these calls reflect a fundamental scepticism about the Rule of Law, as well as a willingness to sacrifice Rule of Law ideals to substantive economic aims.

Is the Rhetoric Likely to Contribute to the Rule of Law?

Two claims about this rhetoric that have been raised above are i) that the 'property rights-Rule of Law' strand tends to limit itself to an economistic emphasis on the creation of secure private property rights which individuals can trade in market transactions and can be enforced in court, and ii) that the strand concerned with limiting government discretion tends toward an opposite extreme of being so vague that the Rule of Law becomes somehow synonymous with good governance. Both of these facts are unfortunate for those concerned with the Rule of Law as an end in itself.

The vision behind the 'property rights-Rule of Law' rhetoric seems to see the ideal society as one governed by two forces, the market and a framework of legal rules and rule-like norms, that provide clear, objective guidance around which, or within which, private market actors can orient their behaviour. In this sense the rhetoric has moved beyond simplistic visions of a self-regulating market, but still leaves little or no room for legitimate judicial or bureaucratic discretion. This is unfortunate because it is so obviously inaccurate as a description of any advanced economy (Davis, 1969) that it can be easily dismissed by political leaders in countries that one might hope would be moving toward a Rule of Law.

Another major problem with this approach is that it does little to prevent authoritarian governments ruling over market economies from claiming that they are Rule of Law societies, when in fact these are simply societies ruled by leadership committed to private property for political/economic reasons, but with no commitment to being governed by law themselves. This tends to reproduce Cold War-era attempts to distinguish Left from Right dictatorships, since many of the latter would enforce a Rule of Law at this level. But what Locke wrote of law in the absolute monarchies is instructive here:

> [T]he Subjects have an Appeal to the Law, and Judges to decide any Controversies, and restrain any Violence that may happen betwixt the Subjects themselves, one amongst another. [But] 'this is no more, than what every Man who loves his own Power, Profit, or Greatness, may, and naturally must do, [to] keep those Animals from hurting or destroying one another who labour and drudge only for his Pleasure and Advantage, and so are taken care of, not out of any Love the Master has for them, but Love of himself, and the Profit they bring him. For if it be asked, what Security, *what Fence* is there in such a State, *against the Violence of Oppression of this Absolute Ruler*? The very Question can scarce be born (Locke, 1960:371).

Seeing the Rule of Law in terms of the enforcement of particular statutory regimes raises additional issues, as the experience of Northeast Asia shows.

The region provides an important early example of globalization in areas like competition and intellectual property law, whereby countries were pressured to adopt formal law inconsistent with their strategic economic policies. When this occurs the Rule of Law is bound to suffer, as subversion of the formal law becomes a necessary, if unstated, component of government economic policy. That this is at least part of the story of legality in Northeast Asia seems clear, and suggests that the best strategy for fostering the Rule of Law might include a good deal of tolerance of divergent substantive policies among legal regimes, so that governments are not forced by the internal logic of their own policies to undermine enforcement of the formal law.

The prevailing vagueness in the Rule of Law rhetoric presents different sorts of problems. Vagueness invites objections based on critiques of the claimed universality of 'Western' values, one of which is the Rule of Law. Just as has occurred in the field of human rights, if grandiose terms are not broken down into specific issues, the way is left open for claims that there are one or more equally valid 'styles' of human rights, or of the Rule of Law. If, however, one raises a concrete issue, such as whether people should be subject to arrest or other legal harassment for peacefully criticizing their government, then culture-based arguments tend to lose their rhetorical effectiveness. If people and institutions are serious about advancing particular elements of the Rule of Law around the world, they should enunciate clearly what those elements are, so that they can be evaluated individually on their merits. This will have the added benefit of encouraging consistency in the positions of those advocating the Rule of Law, so that they do not undercut the credibility of the entire effort by advocating inconsistent positions.[66]

Finally, it is legitimate to question some of the more extravagant claims about the Rule of Law in economic development, even if one believes that the Rule of Law is a worthy aspiration. One could take the position that the more extravagant claims do no harm, and may actually do some good, so why bother contesting them? There are problems with this approach, however. China's leadership, for example, knows perfectly well the growth trajectories of countries like South Korea and Taiwan, which grew dramatically in decades when any comprehensive Rule of Law was lacking.[67] They may well be convinced that a certain level of legalization or legal infrastructure is crucial for continued economic development, but as people raised on Marxism they are fully cognizant of arguments that such a legalized society, as it develops economically, will eventually evolve into a liberal, rights-based society. This is what the hopes for, and fears of, 'peaceful evolution' are all about. Exaggerated claims for the economic necessity of the Rule of Law could thus be seized upon by Chinese

conservatives as evidence that international organizations such as the World Bank are being used as Trojan Horses by Western opponents of China's political system.

If no particular form of the Rule of Law is necessary for economic development, some Rule of Law is certainly a necessary condition for representative democracy, as aspirations of the Rule of Law seek to ensure that the rules and policies enacted by the legislative branch are enforced as intended, and that the government cannot act against a citizen except pursuant to authority granted to it through democratic means. But the argument that a Rule of Law in the limited sense of a legalized system of property rights will evolve into liberal, representative democracy, though attractive, is basically speculative, and clearly open to manipulation.[68] We certainly want to believe the State Department when it promises that 'the rule of law in trade has spill-over benefits elsewhere,' but we should ask ourselves whether we can name a nation in which a just and democratic Rule of Law has evolved smoothly out of a system in which the Rule of Law meant only that private property rights were protected by a system of courts and rules. South Korea and Taiwan have made great strides toward democracy, but it is only possible to see this as an inevitable evolution based on a growing middle class, etc., if one adopts an extremely wide-angle and deterministic view of history, one in which the contingencies and human agency involved in, for example, the 1987 democracy movement in Korea, are ignored. And it may be that in the rush to create the private interests to propel this evolution we will create private concentrations of wealth that have no interest in a general Rule of Law, but find they are better served by non-legalized relations with other private parties and with the State. If the Rule of Law is what we care about, it might be preferable to demand less in the way of deregulation and privatization, but to pay more attention to the legalization of the relationships and procedures that tie governments to private actors. A functioning Rule of Law requires a civil society that is willing to resort to legality, and is used to doing so, in its relations with the State. Mass privatization and deregulation may not be the best way to foster such a civil society, and may in fact work against it. Again Northeast Asia provides a valuable example: an administrative procedure law was debated in Japan for decades, but it was apparently not until the 1980s or 1990s that Japanese business interests put their political muscle behind such a basic element of the Rule of Law in the modern administrative state.

CONCLUSION

US Federal Reserve Board Chairman Alan Greenspan (1998) seized the opportunity provided by the Asian financial crisis to proclaim that '[t]he current turmoil in East Asia ... appears to be an important milestone in what evidently has been a significant and seemingly inexorable trend toward market capitalism and political systems that stress the rule of law (Greenspan, 1998).' Chairman Greenspan may be right about the trend, but in the light of three decades of high-speed economic growth and social progress in much of East Asia, how do we reconcile Greenspan's view with claims that the Rule of Law is necessary for economic development? This chapter has sought to approach this seeming contradiction by bringing up examples from the Northeast Asian experience that call into question the necessity, and in some cases the appropriateness, of a strong version of the Rule of Law in all areas of the economy. The point of this is not to disparage the Rule of Law as a political ideal, but rather to encourage intellectual inquiry, and to suggest why some in developed and developing East Asia might find the Rule of Law-economic development rhetoric unpersuasive. Perhaps the Rule of Law as understood by the development community doesn't include all aspects of the Rule of Law that are familiar to lawyers, but in that case perhaps institutions such as the World Bank should use more care when choosing their rhetoric. This suggests a corresponding responsibility on lawyers not to abstain from this debate, however, unless we are willing to see a central normative concept of our tradition trivialized. Weber (1968:1465, fn. 14) long ago called the idea that Roman law promoted capitalism 'nursery school lore.' Perhaps he would be amused that statements of his on the relationship between capitalism and legal formality have achieved the same status in the Rule of Law-economic development literature, as it relies on Weber, North, Olson, *et al.* to tell the world what form of legal system is 'demanded' by a market economy.[69]

In a broader sense, those who study law in Northeast Asia must be aggressive in using their empirical knowledge to test universalist claims in the social sciences generally, not simply in law, or in the relationship between law and economic development. Given its economic success, any global theory addressing economic issues must be fully compatible with the actual history of modern Northeast Asia. The most important task for those interested in the Rule of Law and economic development is to develop an understanding of the Rule of Law that can be effectively distinguished from the simple legalization of society, or from the suppression of government discretion in economic governance. A legal infrastructure is certainly a necessary precondition of any worthwhile Rule of Law, but the latter will not necessarily evolve out of the former.

NOTES

1 '[I]t is an accepted fact that the weakness of the [Peruvian] judicial system has been an obstacle to that growth, discouraging investors and innovative economic activities while contributing to a general sense of insecurity' (World Bank, News Rel: No 98/1555/LAC).

2 'The first lesson from the Asian crisis is that a government that is not answerable to its people will not be likely to have open markets or the institutions required to impose discipline to overcome a financial crisis. A second lesson is that *guanxi*, or connections, are never a substitute for the rule of law' (Lee, 1998:8).

3 'Rules are there for a reason. In the United States, we do business under a lot of annoying regulations that require company managements to report profits and losses accurately, that prevent banks and those they lend to from getting too friendly, and so on. And we also made it hard for government officials and businessmen to strike deals without a lot of lawyers present. In Asia, they scoffed. They did business on the basis of personal relationships, not narrow legalisms. And now we know the results' (Krugman, 1998:6A).

4 'Developmental state' is used broadly here, to refer to the approach to state-society relations in post-World War II Japan, South Korea, and Taiwan pioneered by Chalmers Johnson, then enhanced and qualified by Alice Amsden, Richard Samuels, Robert Wade, Peter Evans and others. (Johnson, 1982; Amsden, 1989; Samuels, 1987; Wade, 1990; Evans, 1995).

5 '[T]he rule of law may not be a single concept at all; rather, it may be more accurate to understand the ideal of the rule of law as a set of ideals connected more by family resemblance than by a unifying conceptual structure' (Solum, 1994).

6 The following is a list of some of these concerns according to the aspect of the legal process in which they arise:
Positive Law: The positive law should be clear and knowable in advance, so that citizens are not held liable, civilly or criminally, based on legal rules of which they could not, through normal means, have been aware. The legal norms must be of general applicability, rather than being directed toward individuals.
Judiciary: In deciding cases, the judge should have no personal interest in the matter, should not prejudge the matter, and should decide a case by applying the pre-existing law to the facts as developed during the proceeding. Like cases should be decided alike, and the judge should not be influenced by non-legal substantive or instrumental considerations.

Basic procedural rights, such as a right to be heard and to contest adverse evidence, are also presumed.

Executive Branch: Officials of the executive branch should have pre-existing legal authority for any action they take that affects private rights. This means both that officers should have been granted a general statutory authority to act in a particular field, and that such action, when taken, should not exceed the scope of any discretion that has been granted to the officer.

7 Dicey's famous mischaracterization of the French *droit administratif* in comparison to the English Rule of Law is instructive (Dicey, 1982; Hayek, 1960).

8 Formalist in its assumption that the materials and methods of the law are sufficient to provide single correct answers to particular legal issues; positivist in the assumption that the materials of the law consist primarily of rules and rule-like social norms not subject to significant indeterminacy, and that these are sufficient to provide single correct solutions without resorting to principles, policies or purposes.

9 This admittedly impressionistic view was gleaned from a reading of the Rule of Law-economic development literature cited herein, which makes regrettably few efforts to define the Rule of Law. One definition that did appear was from Hayek, 1944. '... this means that government in all its actions is bound by rules fixed and announced beforehand – rules which make it possible to foresee with fair certainty how the authority will use its coercive powers in given circumstances and to plan one's individual affairs on the basis of this knowledge' (Dhonte and Kapur, 1996). Another work defines the Rule of Law as reflecting 'the degree to which the citizens of a country are willing to accept the established institutions to make and implement laws and adjudicate disputes.' (Knack and Keefer, 1995). Knack and Keefer take their definition from the International Country Risk Guide, a privately produced political risk guide marketed toward multinational investors, which had originally used the pithy 'law and order tradition' to describe this variable (Knack and Keefer, 1995:225).

10 Important current examples are Douglass North (economist), Mancur Olson (economist), Jeffrey Sachs (economist), and Barry Weingast (political scientist). Two pioneers in this tradition, Max Weber and Friedrich Hayek, were exceptions.

11 (North, 1990). On bounded rationality generally, see Conlisk (1996).

12 As noted above, this chapter was prompted by the seeming general explosion of Rule of Law language in publications dealing with economic development, not simply its use by the World Bank or another particular institution. It seemed appropriate, therefore, to look at many

sources, rather than simply analysing one particular document. The danger of this approach is that one could easily select only those sources that support one's argument. I can only say that I have tried to avoid doing so.

13 Many of the sources consulted for this chapter discuss two or more of these concerns, but I have tried to separate them for purposes of analysis.

14 Perhaps not surprisingly, these concerns track exactly Locke's explanation of how property was inadequately protected in the State of Nature: want of '*establish'd*, settled, known Law,' want of a '*known and indifferent Judge*, with Authority to determine all differences according to established Law,' and want of 'a *Power* to back and support the Sentence when right, and to *give* it due *Execution*' (Locke, 1960).

15 A truly disturbing over-emphasis on such criminal law aspects is found in Posner (1998).

16 'Property rights are at the heart of the incentive structure of market economies. They determine who bears risk and who gains or loses from transactions. In so doing they spur worthwhile investment, encourage careful monitoring and supervision, promote work effort, and create a constituency for enforceable contracts' (World Bank, 1996:48-9).

17 '[W]ell functioning markets also need a clear sense of where the state's role ends. The government must itself be ruled by law and trusted by private entities not to intervene arbitrarily in their affairs, to follow its announced policy statements, and to deliver on its obligations' (World Bank, 1996:93-4).

18 North (1990:139) writes, 'The security of property rights and the development of the public and private capital market were instrumental factors not only in England's subsequent rapid economic development, but in its political hegemony and ultimate dominance of the world.' Olson is no less adamant: 'With a carefully constrained monarchy, an independent judiciary, and a bill of Rights, people in England in due course came to have a relatively high degree of confidence that any contracts they entered into would be impartially enforced and that private property rights, even for critics of the government, were relatively secure. Individual rights to property and contract enforcement were probably more secure in Britain after 1689 than anywhere else, and it was in Britain, not long after the Glorious Revolution, that the Industrial Revolution began' (Olson, 1993:574).

19 'If organizations – firms, trade unions, farm groups, political parties, and congressional committees to name a few – devote their efforts to unproductive activity, the institutional constraints have provided the incentive structure for such activity. Third World countries are poor

because the institutional constraints define a set of payoffs to political/economic activity that do not encourage productive activity' (North, 1990:110).

20 'If political transaction costs are low and the political actors have accurate models to guide them, then efficient property rights will result. But the high transaction costs of political markets and subjective perceptions of the actors more often have resulted in property rights that do not induce economic growth, and the consequent organizations may have no incentive to create more productive economic rules' (North, 1990:52).

21 It will only be noted here that this depoliticization of the very core of politics – private rights, the separation of powers, and checks and balances – is also necessary if international financial organizations are to comply with prohibitions typically found in their charters against interfering in the domestic political affairs of their member states.

22 'Although many of the structural reforms that the IMF included in its early-December [1997] program for Korea would probably improve the long-term performance of the Korean economy, they are not needed for Korea to gain access to capital markets. They are also among the most politically sensitive issues: labor market rules, regulations of corporate structure and governance, government-business relations, and international trade. The specific policies that the IMF insists must be changed are not so different from those in the major countries of Europe' (Feldstein, 1998:27-8).

23 These rights do not differ fundamentally from those discussed in the previous section, and are also often justified on economic grounds. They are treated separately here because they tend to be advocated by different Rule of Law publicists, for example, the United States Trade Representative (USTR) rather than the World Bank, and they are often supported more directly by international obligations.

24 Former USTR Mickey Kantor made this connection between IPR enforcement and the Rule of Law when describing the 1995 US–China agreement on IPR enforcement: 'The essence of that agreement, and all our trade agreements, is respect for the rule of law. The IPR agreement promotes citizen access to the judicial process, by requiring China to publish relevant laws, and standards, and by requiring the creation of guidebooks to the enforcement system. The IPR agreement applies these principles in a commercial sphere, but its ramifications for China go far beyond patents and trademarks.' Statement of Ambassador Michael Kantor, Prepared for Delivery to US–China Business Council, 31 January 1996 (transcript on file with the author).

25 'The US Customs service, the FBI, Department of Justice, Patent and Trademark Office, the Department of Commerce and the US Information Agency have all offered training – and will continue to do so. Chinese prosecutors and Chinese Customs officials are receiving training right now in facilities in the United States and China. US industries have been equally generous.' Statement of Ambassador Michael Kantor before the Senate Foreign Relations Subcommittee on East Asian and Pacific Affairs and the House International Relations Subcommittees on Asia and the Pacific and International Economic Policy and Trade, 7 March 1996.

26 Perhaps the Rule of Law in China will then 'spillover' into the State Department's exercise of its authority to issue tourist visas, which a Federal District Court found to be illegal (Bureau of Public Affairs, 1997). See *Olsen v. Albright*, 990 F. Supp. 31 (D.D.C. 1997) and Shenon (1998:1).

27 'Formal constraints on arbitrary state power in established market economies derive partly from constitutional and administrative law. These bodies of law ensure that all legislation is consistent with the national constitution and that regulations, in turn, are consistent with the law. They delineate the rulemaking authority of various state bodies, lay out the procedures for enacting laws and promulgating regulations, and provide individuals recourse against unlawful or capricious state action' (World Bank 1996:94).

28 A useful introduction is Faber and Frickey (1991).

29 'Uncertain rules, heavy regulation, and pervasive controls give officials exceptional power, many opportunities to seek bribes, and wide scope for appropriating public wealth' (World Bank, 1996:95).

30 '[G]overnments are particularly susceptible to corruption during the phase when the state retains both vast assets and extensive powers to intervene in a growing private economy. Liberalization, demonopolization, and – if transparent – rapid privatization are key steps to reducing these two sources of huge economic rents and to strengthen demand for the rule of law' (World Bank, 1996:144).

31 Corrupt practices could also occur in other government activities, including the regulation of private sector activities that do not have a direct impact on the budget or public finances, such as ad hoc decisions made in relation to the regulation of foreign direct investment. Such practices would be counter to the IMF's general policy advice aimed at providing a level playing field to foster private sector activity' (IMF, 1997:par 10).

32 An exception to this general pattern is, World Bank (News Rel: No. 98/1515) 'Noting that corruption and financial crises flourish in the

dark, Wolfensohn said that, irrespective of political systems, public decisions must be brought into the light of public scrutiny. This is not a luxury: this is a fundamental prerequisite for maximizing growth and poverty reduction.'

33 '[T]he East Asian example would seem to suggest that high levels of economic performance bear little or no relation to the development of a credible legal system' (Jayasuriya, 1999).

34 See, Greif (1996) and Greenhalgh (1988). In an example of economic dogmatism, one of the IMF's prolific writers on governance and economic performance defines corruption as 'noncompliance with [the] principle of the arm's length relationship, which states that *personal or family relationships ought not to play a role in economic decisions by private economic agents* ... This principle is essential for the efficient functioning of markets.' Summary of Vito Tanzi, Governmental Activities, and Markets (IMF Working Paper WP/94/99-EA) (visited Nov. 24, 1998) (emphasis added). Given the importance of family businesses in pre-World War II Japan, and in post-World War II South Korea and Taiwan, Tanzi's statement can only be taken to mean that 'the efficient functioning of markets' is not necessary for economic development.

35 'The monopolist cannot only do without calculable law, formal rationality is even a fetter to the full development of his power. The rational law has ... not only the function of rendering exchange processes calculable, it has an equalizing function also. It protects the weak. The monopolist can dispense with the aid of the courts; he does not go to the courts. His power of command is a sufficient substitute for the coercive power of the state' (Neumann, 1986:282).

36 South Korean president Kim Dae-Jung has 'called for an improvement in the relationship between *chaebol*s and small companies by which large enterprises can no longer rule or dictate over small ones.' Hyoung-min Kim, 'Pres.-Elect, Chaebol Owners Agree on Reform', *Korea Times* 13 January 1998.

37 The World Bank makes strong claims in this regard. 'Most day-to-day contracts in market economies do not require formal enforcement. ... But an economy still needs credible, low-cost formal enforcement mechanisms to which aggrieved parties can turn when all else fails' (World Bank, 1996:90).

38 'The inevitable conclusion that one arrives at in a wealth-maximizing world is that complex contracting that would allow one to capture the gains from trade in a world of impersonal exchange must be accompanied by some kind of third-party enforcement' (North, 1990:57) 'The shortage of institutions to enforce contracts limits the scope of

transactions, makes contracting more costly, and prohibits some contracts altogether' (World Bank, 1996:90).

39 This is changing in Japan and South Korea, where the legal regimes have been amended to make shareholder derivative actions more attractive to litigants. This is clearly an important change; how it will effect the Japanese and South Korean economies remains to be seen.

40 Anyone trying to predict the future path of corporate governance in China should note that government's interest in the South Korean *chaebol* model. 'Hu Xiongfei, deputy director of the Shanghai Economic Commission, voices an opinion held by many Chinese officials: 'These *chaebol*s contributed a lot in transforming Korea from an agricultural country into an emerging industrial one, with GNP increasing from US$2.1 billion in 1961 to US$480 billion in 1996' (Yatsko, 1998).

41 The OECD explains the need for its proposed Multilateral Agreement on Investment (MAI) as follows: 'While markets are, of course, the main reason for investment decisions, the investment climate is also a major factor in decision-making. Investors need long-term stability of rules and procedures. They need open markets and equal competitive opportunities with domestic investors' (OECD Policy Brief No. 2-1997).

42 The International Country Risk Guide's original variable, 'law and order tradition,' thus seems to more accurately describe the state of affairs their clients value (Knack and Keefer, 1995:225).

43 Mancur Olson, perhaps in a nod toward South Korea and Taiwan, acknowledges that some dictatorships have presided over periods of exceptional economic growth by providing secure property and contract rights absent democracy or the Rule of Law. He argues, however, that such growth cannot last because the rights provided by a dictator are not sufficiently secure in the long run (Olson, 1997:572-2).

44 China's Hunan Province reportedly has a back-log of 100,000 unenforced commercial verdicts, dating back to 1992. 'Court Delays Force Chinese Litigants to Turn to Gangsters' *Agence France-Presse*, 2 December 1997 (quoting the Worker's Daily).

45 The tale of foreign investment in the Chinese telecoms industry provides a fascinating example. The world's top telecom companies invested US$1,400,000,000 in China's telecoms service industry via complicated contractual arrangements designed to circumvent a ban on foreign investment in that sector. The existence of the ban was known, but investors relied on the 'repeated blessings of top Chinese officials.' James Kynge, 'Blow for telecoms investors in China', *Financial Times*, 22 September 1998, at 8.

46 'Many European, Asian and some American lenders overlooked the inadequacies of the Indonesian legal system and decided to put their trust in their debtors' connections ...' (Paal, 1998:6).

47 Indeed, IMF, World Bank, and International Finance Corporation interest in Indonesia's bankruptcy law appears driven by a desire of foreign investors to limit losses on investments they have already made. Thoenes, Sander, 'Indonesian Bankruptcy Law Dealt Fresh Blow', *Financial Times*, 25 November 1998, at 4.

48 The same point could be made with regard to negotiations over China's accession to the WTO.

49 Government exercises of discretion here might be analysed through the lens of 'administrative guidance,' but discussions of administrative guidance in the abstract can be more confusing than enlightening. The propensity to regulate through informal rather than formal means is probably inherent in modern bureaucratic governance. For an inquiry into the Rule of Law in Northeast Asia the interesting questions include, i) whether government actors possessed means to enforce their informal 'guidanee' that are contrary to the Rule of Law, and ii) whether they exercised guidance over the economy that was central to the 'developmental state.'

50 A good discussion of the 'traditional' Japanese system, and how and why that system is becoming more legalized, is Masaru Mabuchi (1993:130).

51 The fundamental debate concerns whether policy lending was conducted by relatively insulated technocrats in such a way as to exert effective guidance over the path of economic development, or whether such loans should be better understood as part of a corrupt government-business cycle in which loans were obtained in exchange for political contributions, which were obtained in exchange for loans, and so on.

52 Economists have been more concerned with the effects of policy lending, and whether growth would have been even faster in Northeast Asia if credit allocation had been left more to market forces.

53 In 1993, Korea's Constitutional Court held that the destruction of the *Kukje* Group was unconstitutional, invoking the Rule of Law as a check on government action necessary for legal security and predictability in the economic realm. The Kukje case and its possible implications are discussed in James M. West, *Kukje and Beyond: Constitutionalism and the Market* (June, 1998) (unpublished manuscript, on file with the author).

54 A typically cynical 'new institutionalist' discussion of foreign investment screening is Thomas W. Waelde, *A Requiem for the 'New*

International Economic Order', 1 CEPMLP On-Line Journal 2 (June, 1995) <http://www.dundee.ac.uk/petroleumlaw/html/article1-2.htm>.

55 '[T]hose charged with the application and enforcement of the Foreign Investment Law and the regulations thereunder possess virtually unreviewable power to control inward capital investments. Much of the law and regulations have left to government administrators the discretion to fashion the details and working policies by which validation applications are screened. For the most part, such applications are judged by current economic and political considerations rather than by precise standards and rules formulated in statutes, cabinet orders and court decisions' (Hartman, 1972:376). The OECD's proposed MAI would make it very difficult for any developing country to follow the 'developmental state' model for screening foreign investment by i) concerning itself with the making of investments, not just the treatment of investments once made, ii) requiring 'national treatment' for foreign investors, iii) requiring 'most-favored-nation' treatment for foreign investors, iv) requiring that laws, regulations and procedures of general application be publicly available, and v) prohibiting performance requirements. In return, parties to the MAI 'will enjoy the benefits of a better investment environment' OECD (1997).

56 Some investors are more candid than others about investing in Asia and the Rule of Law. Founder of the failed Peregrine investment bank, Philip Tose, reportedly 'went out of his way to emphasize an "Asian way" of doing business. This included contempt for democratic countries that he viewed as unlikely to make economic progress. He publicly preferred to deal with authoritarian governments, holding in contempt India, Australia and the Philippines, where democracy and the rule of law operated, however inadequately.' Philip Bowring, 'Wake-Up Call from Peregrine to Bankers Everywhere', *International Herald Tribune*, Wednesday, 14 January 1998, at 8.

57 As one commentator notes, 'national treatment,' which like the Rule of Law goes to the administration rather than the scope of regulatory authority, 'means little to a foreign investor if the treatment meted out to national companies is below *reasonable standards of state regulation* ('international minimum standards') in developed countries. The criterium of national treatment, in our view, is therefore only a stopover...' (Waelde, 1995: par 44) (emphasis added).

58 Typical is the report that Taiwan's tax authorities, as part of a government effort to defend Taiwan's currency, have threatened to 'look into those [financial institutions] that might have profited from "speculation".' Chad Rademan, 'Taipei Banker Gets Tough to Uphold Currency,' *International Herald Tribune*, 18-19 April 1998, p. 17. The

Rule of Law ideal would seem to demand that trading activities be subject to a system of rules defining what is allowed and what is not allowed, and that the government not be able to discourage allowed activities by threatening tax audits or similar measures.

59 Discussions of administrative guidance in Japan often mention almost as an afterthought that those giving the 'guidance' have this tool to coerce compliance, as if it is less important than, for example, the identity of interests between regulators and regulated that is presumed to arise out of Japan's corporatist regulatory system (Akira, 1985:279).

60 One standard American analysis of Japanese administrative guidance calls this 'collateral enforcement,' and wastes little ink on Rule of Law concerns (Young, 1984). This non-judgmental relativism seems to be the norm in academic writing on administrative guidance, at least in the US.

61 Fallon (1997) identifying four Rule of Law 'ideal types' within US Constitutional law discourse alone.

62 This also ignores the related problems of whether the aspirations that make up the Rule of Law in this approach have much to do with how actual cases are decided, or whether such higher level aspirations, if they are important in judicial decision making, are in fact neutral and just, or simply reflect existing social relations.

63 (Pound, 1942). Much important twentieth century legal scholarship has in fact been driven by the difficulty of reconciling Rule of Law ideals with the modern governance. See, Neumann (1986), Davis (1969), Lowi (1969), and Sunstein (1990).

64 The view of the judge implied in the Rule of Law-economic development literature seems inspired by Weber's implausible claim that 'the judge ... in the bureaucratic state with its rational laws, is more or less an automaton of paragraphs: the legal documents, together with the costs and fees, are dropped in at the top with the expectation that the judgement will emerge at the bottom together with more or less sound arguments – an apparatus, that is, whose functioning is by and large calculable or predictable' (Weber, 1968).

65 Marcus (1998:A01) describing property rights education seminars for US federal judges sponsored by the Foundation for Research on Economics and the Environment (FREE), a foundation funded by conservative groups that also fund legal challenges to regulatory limitations on absolute property rights.

66 A notorious example of this was the US government's support for arguably authoritarian measures by the government of China to reduce IPR infringement, including the registration of all printing facilities.

67 The effectiveness of China's foreign investment screening system, which shares much with the systems employed by South Korea and Taiwan, is testified to by the fact that it has become a matter of political concern in Washington (Office of Strategic Industries and Economic Security, 1999).

68 In these aspects, the argument resembles the '*deux-commerce*' thesis of the eighteenth century, which held that 'the market and capitalism were going to create a moral environment in which a good society as well as the market itself were bound to flourish' (Hirschman, 1992). Like the *deux-commerce* thesis, current evolutionary arguments are an important part of a complex reality (Hirschman, 1992:139).

69 The core 'Weberian' claim appears Weber (1968:1393-5) (Appendix II, ii: Bureaucracy and Political Leadership).

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