

## Rewriting the Rules of the Game in Russia: The Neglected Issue of the Demand for Law

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As a Hollywood movie put it, “if you build it, they will come.” This catchphrase captures the flavor of the assumptions underlying legal reform in Russia over the past decade. Recognizing that, to a great extent, law had been marginalized during the Soviet period, domestic policymakers and their foreign advisers identified two key reasons why Russians shied away from using the law to protect and advance their interests. The first centered on the well-chronicled shortcomings of Soviet law, apparent in both its generally poor quality (for example, rampant internal inconsistencies, its declaratory character, lack of transparency) and the politicization of legal institutions by the Communist Party. The second reason lay in the absence of key incentives, primarily private property, the existence of which—it was reasoned—would lead individuals and firms to desire and use law to protect their newfound property interests. From this line of thinking, it presumably followed that if these problems were fixed and the “correct” laws and legal institutions were put into place, then Russian citizens would begin to make use of them. Although this connection between supply of and demand for law may have seemed self-evident, it has proven elusive in practice.

To be sure, Soviet-era reluctance to mobilize law was, in part, a product of dissatisfaction with laws that often contradicted one another and with the adminis-

trative acts, or *podzakonnye akty*, that complicated their implementation, not to mention abiding doubts about the courts’ independence. Certainly, reforms aimed at remedying these legacies of the Soviet legal system represent a step forward. Moreover, private property has elsewhere proven to be a powerful engine for legal development. But merely rewriting the “rules of the game,” while undoubtedly a necessary prerequisite to stimulating a demand for law, has not sufficed—given the absence of efforts to address the more deeply rooted causes of Russians’ antipathy toward law. Decades of watching law being used in a crudely instrumental fashion in order to serve the various ends of the Communist Party have taken their toll. Similarly, the obvious ability of the party elite to manipulate the outcome of court procedures led many to conclude that power trumps law, that “telephone law” is more potent than written legislation.

Not surprisingly, then, Moscow’s embrace of the rule-of-law state (*pravovoe gosudarstvo*), beginning with Gorbachev and continuing with Yeltsin, has been greeted with considerable skepticism by ordinary citizens. The idea that law could be used by ordinary citizens to protect themselves from arbitrary or illegal actions by the state or to advance their own interests in private transactions was viewed as unrealistic in the post-Soviet context. Such attitudes are unlikely to

change quickly. Even though the Communist Party has been stripped of its monopoly on power, most feel that overweening political power has been exchanged for a comparable economic power. From the outside, the system may look different, but to citizens, the bottom line is the same. The powerful are able to manipulate both the substance of law and the outcome of specific cases. Whether these perceptions are borne out by contemporary reality is still open to question. But they have to be recognized as a powerful constraint not just on meaningful legal reform but on the demand for law itself regardless of how good the "supply" may be. As things stand now, citizens are unlikely to respond immediately to overblown rhetoric about the importance of establishing a *pravovoe gosudarstvo*, or even to changes in the letter of the law, whether legislative or institutional. The Soviet legacy of campaigns in which such changes were announced with great fanfare only to be forgotten when the noise died down created a situation where Russians judge by deeds not words. They will adapt their behavior to the legal system only when they are convinced that the law is potentially useful to them.

### **Building a new legal system**

Comparing snapshots of the legal landscape in 1985 and in 1998 would make immediately apparent the fundamental and far-reaching nature of recent reforms. A full catalogue of the changes is beyond the scope of this article, but a few deserve singling out. Even before the Communist Party was divested of its power, its influence (at least on a formal level) over the courts of general jurisdiction had deteriorated. Indeed, the judicial branch is finally out from under the thumb of the Ministry of Justice and has become self-governing. A constitutional court has been created and, after a bit of a false start, has begun to find its own voice; for example, the court has shown a willingness to take on thorny political issues affecting both Moscow and the regions. Economic (or *arbitrazh*) courts, which deal with commercial disputes, have been established on the institutional foundation of the Soviet-era *gosarbitrazh* (which lacked the accoutrements of a court and functioned more like an administrative agency). In addition, the number of new law-related institutions that have been created rivals Roosevelt's record during the early New Deal

years. Agencies have been founded to assist in the implementation of antimonopoly, bankruptcy, securities, privatization, and other laws. Judged in quantitative terms, the legislative output during this period has also been extraordinary. Laws have been passed that institutionalize various features of the market economy and the democratic political order. Principal among these are the Constitution, and the criminal and civil codes.

Returning to the basic premise of the reformers, can we say that the supply of law has been, or should have been, adequate to stimulate demand? In pondering this question, we need to be realistic in our expectations. No legal system is ever fully realized. Inevitably, progress is piecemeal and relative. The goal is not perfection—not a flawless *pravovoe gosudarstvo*—but adequacy. Are enough of the necessary laws and institutions in place such that Russian citizens are able, in principle, to mobilize their rights in relation to both private and state actors? The answer to this question is a resounding yes. On paper, Russians enjoy a relatively full panoply of rights (both civil and economic), and the procedural mechanisms exist to permit their exercise. (The laws are neither ideal nor enforced in full measure; but they are on the books.) The reformers' position has been that the "building" of this new and improved legal system, replete with enforceable property rights, is a sine qua non for stimulating an increased use of the law.

### **Mobilizing law in post-Soviet Russia**

But what is the reality? To what extent have the reforms of key laws and legal institutions given rise to increased use and thus stimulated demand for yet more law? Assessing levels of the use of law and the demand for more law is hazardous at best. Statistics document, over the past few years, increased caseloads of both the courts of general jurisdiction and the *arbitrazh* courts. But these cases undoubtedly represent the tip of the iceberg of potential disputes, and so drawing general conclusions from these data is not prudent. They indicate only that some individuals and firms are using legal institutions to resolve their disputes. But the same could be said of the Soviet period.

Demand might also be judged by the participation of society in the lawmaking process and the level of agita-

tion for new laws and legal institutions coming from citizens and grassroots organizations. But with certain notable exceptions, legal reform has been top-down. Many of the reforms draw heavily on examples from abroad, with foreign advisers often participating actively in the drafting process. All too often the drafters' preoccupations were more with technical perfection than with how concepts borrowed from elsewhere would interact with Russia's own preexisting law and legal culture. This was most evident in the realm of economic law but was a persistent feature apparent in the overall legal reform effort. To be fair to the reformers, there was no hue and cry from ordinary citizens to be included in the process, while there was enormous pressure, generated both internally and by foreign donors, to move swiftly. As might be expected based on their historical experience, ordinary Russians took little interest in new laws and institutions.

This apathy toward law is not surprising. Indeed, rather than materializing spontaneously within Russian society at large, the demand for law is likely to emerge first among economic actors. Their payoff for using law is more readily apparent than benefits to other groups. Remedies for contractual breaches are more tangible than the merely moral satisfaction that results from prevailing in a criminal or human-rights claim. Outside the realm of litigation, a properly functioning legal system, based on clear, evenhanded norms, can greatly reduce transaction costs for businessmen. Russia's reformers actually agree with this point, though for different reasons. They contend that the impetus for further legal change will come from those groups within society that have obtained significant amounts of property through the privatization process. Prominent among such groups are enterprise managers. Examining their attitudes and behavior may provide some insight into the broader question of the demand for law.

Given the heavy weight of the past on the present in Russia, it is important to acknowledge our starting point. During the Soviet period, enterprise managers did not rely primarily on law to protect their interests. This is not to say that law did not exist. On a superficial level, law was used extensively. Enterprises memorialized their trading relationships in the form of contracts and brought claims against one another with considerable regularity in *gosarbitrazh* (though this

served more as a signaling device to ministries than as a mechanism for resolving bilateral disputes). But the contractual form was largely empty of substance. Legal niceties mattered less than plan fulfillment. Enterprise managers understood that their protection depended not on the force of law but on their political connections and their ability to bring pressure to bear on their trading partners. Within the realm of the economy (as in much of the rest of Soviet society), law was not a freestanding bulwark but a malleable instrument available exclusively to the state and the Communist Party elite that stood behind it.

Believing that this way of proceeding was motivated by the political corrosion of the Soviet legal system, reformers anticipated that changing the rules of the game would provoke behavioral changes. These expectations were grounded both in the ongoing qualitative improvements to the legislative base and in the introduction of private property, which gave these managers something tangible to protect. The underlying assumption is that reliance on law is inherently more efficient than the use of political power because the associated transaction costs (in terms of both time and money) are, in theory, so much lower. As a result, the reformers anticipated that enterprise managers, as rational actors, would shift from a reliance on personal connections and patron-client networks to a reliance on the impersonal rules and institutions at the core of the new Russian legal system.

But what is rational may differ in different settings. The experience of Russian managers has not taught them to count on law as a mechanism for maximizing an enterprise's interests. For them, believing in the usefulness of law would require an enormous leap of faith. It is not that these managers do not grasp the Western argument about the efficiency of law. They do. They just do not see the pertinence of this argument and, perhaps, of law itself to their circumstances. The concept of law as a relatively neutral and stable set of norms by which they can organize transactions is foreign to them. On the other hand, the role of law, during the Soviet era, as a handmaiden to politics is well-documented and deeply etched in the Russian psyche. Why should they place their faith in law—and alter their behavior accordingly—when they have so little experience with law as a means of protecting and

advancing their interests and so much experience with law as an instrument of the state? If we put ourselves in their shoes, we begin to understand their hesitancy and resistance to embracing law. When asked why they avoid the courts, managers often reveal their suspicion that extralegal powers will inevitably override a legally correct position. For example, a Moscow auto-parts-factory manager told me that, notwithstanding their huge debts, it was pointless to sue the giant auto assembly plants on their home turf (for example, to sue AvtoVAZ in Toliatti or GAZ in Nizhniy Novgorod). He had no particular evidence for his belief, but his misgivings sufficed to keep him away from the courts. (His reluctance to sue was no doubt also influenced by his unwillingness to risk losing future orders by angering these large auto plants.)

Rather than turning to law, Russian managers prefer to stick to tried-and-true methods of conducting business. When problems arise and negotiation proves fruitless, their recourse is typically not to the courts but to informal mechanisms. Sometimes, this involves protracted negotiations between long-term trading partners. The cash-poor status of many industrial enterprises has given so-called intermediaries, who can dispose of goods acquired in barter exchanges, a more central role. Still another option is turning to political patrons for assistance. In all cases, the goal, as during the Soviet era, is to exert pressure on trading partners in order to force payment of amounts owed. One key difference between the processes now and during the Soviet period is that they have grown even more onerous and time-consuming. This increased difficulty is the result of the rise in barter and the almost constant turnover of personnel within a governmental apparatus buffeted by the shifting winds of power. Patronage networks have become more fragile and tenuous. Moreover, often enough, these networks now extend into the shadowy world of organized crime. Few Russian enterprises are strong enough to survive without some sort of security service, or *krysha* (though some have brought this function in-house). For most, these methods of resolving disputes are preferable to relying on law. Indeed, they may be more efficient, in a real-world sense, because they are more familiar.

### **The low demand for law that is otherwise in reasonable supply**

Let us consider, somewhat more closely, why law should be in such meager demand. A number of reasons come to mind, many of which are suggested by, but resonate beyond, the specific circumstances in which enterprise managers find themselves.

*The potent legacy of Soviet legal culture.* Changing established patterns of behavior is never easy. Inertia sets in; people fall into ruts. This is certainly true of Russian managers. General directors, in particular, know how to manipulate the patron-client system inherited from the Soviet period. They sit at the center of a highly complex web of connections that is largely personal. Ultimate power rests with these directors. Only they can tug on one or another string and expect results. Such a system represents (at least in theory) the antithesis of a reliance on impersonal laws and institutions to resolve disputes without regard to the status of the litigants. But while recourse to law may appear more efficient—since problems can be resolved more quickly—what is less apparent is a collateral loss of power by managers. Accustomed to unquestioned power within the enterprise and in their interenterprise relations, activist general directors are loathe to give up any piece of it. Once a dispute is handed over to the courts, a director can do little but sit and wait for the decision. Before shifting to a reliance on law, directors have to believe that judges and laws are relatively impartial; in other words, that their enterprise has an equal chance to prevail. In the face of such a belief flies both historical experience and the long-standing skepticism of law among Russian citizens.

The shift to a reliance on law makes sense only if it is made almost simultaneously by a substantial majority of potential litigants. Managers are understandably reluctant to be the first to make the move, thereby ceding an advantage to law-adverse trading partners who could still appeal to political or other patrons. The safer option is to stay the course. In this, we find a classic dilemma of collective action. Inured to high-flown if empty rhetoric about “reform,” managers (and others) thus may be waiting for concrete evidence of law’s usefulness. If so, we may find ourselves trapped in a vicious circle. In economic

transactions, the value of law lies in its ability to provide a common language (basic rules and a preapproved forum for resolving disputes) that need not be contested in every new transaction. If, however, significant numbers of potential users persist in bypassing it, then the law loses this critical virtue. Proof of utility will appear only if and when a specific law or legal institution is, in fact, widely used.

*Method of carrying out reforms.* Also important is the way legal reform has been carried out. The reformers had a vision of what was required to make the Russian legal system "normal" and believed they knew best what Russian society needed. This experts-know-best attitude, needless to say, contains troubling echoes of the Soviet past. There is a long tradition, dating back to czarist days, of reform descending from above. This tradition, unfortunately, lives on in post-Soviet Russia. Thus, when designing the legal building blocks of the market economy, such as a civil code or the joint-stock-company law, little effort was made to fathom how existing enterprises were actually doing business. Instead, attention was focused on adapting laws that had worked in other contexts to Russian circumstances (sometimes this may have meant no more than translating other countries' laws). Such an approach ignored the negative experiences of Latin America and Africa, where this path had been followed decades earlier. Simply put "transplanting" laws has all too often been a dismal failure.

Russia's lack of market experience since 1917 has opened up a particularly wide gulf between laws on the books and actual practice. Consequently, the import of sophisticated legal tools has often had disparate effects on various economic actors. Those well trained in market principles have been able to use these new tools to their advantage, while most were merely puzzled. A good example of this disparate impact is the requirement that large companies (those with more than 1,000 shareholders) use cumulative voting to elect members of the board of directors. Institutional investors have used this rule to elect their representatives to the board while worker-shareholders never fully mastered this mechanism, never understood how to use it to their advantage.

For ordinary Russians, the most recent round of legal reform came across as more of the same—as just

another campaign. During the Soviet period, people learned to turn a deaf ear to proclamations of legal innovation, secure in the knowledge that everything would revert to normal in a matter of weeks or months. The persistent inability or unwillingness of the Gorbachev and Yeltsin governments to follow through on reforms and work on the tough questions of implementation has convinced the public that nothing has changed. Enterprise managers and others need to be convinced, in a positive fashion, that law has assumed a new significance. They will not take it on faith.

*Shortcomings in the Russian legal system.* The most often-heard explanation for lack of demand is that Russians shy away from law because the legal system is so flawed. (Delays in the judicial process are routinely cited.) The popular press in Russia fuels this wariness of law with Dickensian tales of simple cases that drag on for years, even decades. Abuses certainly occur. But again, they are an unfortunate fact of life plaguing judicial systems throughout the world. In Russia, the delays are much worse (both in fact and in perception) in the courts of general jurisdiction than in the *arbitrazh* courts. Even so, the official statistics for 1996, indicating that the statutory deadlines for resolving cases were exceeded in 14 percent of cases heard in courts of general jurisdiction and in less than 5 percent of the *arbitrazh* courts, suggest that the problem is less pervasive than critics would have us believe. At the same time, delays cannot be dismissed as unimportant, particularly to a legal system struggling to establish its viability. All too often, justice delayed does indeed amount to justice denied.

Another shortcoming frequently pointed to is the persistent difficulty in getting judicial decisions enforced, particularly in the *arbitrazh* setting. V. F. Yakovlev, the chairman of the higher *arbitrazh* court, has described this as the Achilles' heel of the *arbitrazh* system. After years of delay, legislation has been passed creating the *sudebnye pristavy* (bailiffs), who are to replace and improve upon the service provided by the *sudebnye ispolniteli*. Yet this institutional reform is unlikely to solve the problem permanently. For nonenforcement of judgments has to do less with the competence or resources of those charged with enforcing judicial decisions and more with the ever-mounting debts of enterprises (both to tax authorities

and trading partners). These overwhelming obligations have left companies illiquid and patently unable to satisfy judgments against them (when the insolvency is not a façade, concealing resources diverted elsewhere). If the bank accounts are empty, then the only option is to seize an enterprise's equipment or fixed assets and sell them at auction. No judicial system in the world, however, could take such a broad hands-on approach to enforcing decisions, except under rare and unusual circumstances. High levels of voluntary compliance are the norm elsewhere, but they are the exception in Russia. Once again, we confront a vicious circle. The courts will become legitimate only through widespread use, but using courts that lack legitimacy may not be in the best short-term interests of the parties in conflict.

Flaws in the Russian legal system undoubtedly contribute to the lack of demand for law. But this does not mean that, if the flaws were eliminated, demand would automatically materialize. As I noted above, many shortcomings already have been remedied, and yet demand remains elusive. The reality is that all legal systems are riddled with flaws, either more or less serious than those in Russia, and yet they are not plagued by the level of apathy and doubt regarding law that is all too commonplace in Russia. It has become increasingly apparent that there is a fundamental misalignment between the new "rules of the game" and the game itself. What works in Western Europe or in the United States may be inappropriate for Russia, where market relations are still in a formative period. Yet reformers seem to have deliberately put into place laws that did not reflect how business was actually being done but rather how the reformers would like to have seen business being done. Presumably their motive was to bring Russian law into line with that of the advanced industrialized world and thereby to pull the country into the global market. But the gap between the ideal of the reformers and the reality of Russian enterprises was and still remains too wide. This disconnect between legality and reality can only confirm average Russians in their ingrained, lifelong habit of skepticism toward law.

*Lack of legitimacy of the Russian state.* If law is to become a societal touchstone, then it has to be applied in equal measure to all, regardless of power or status. Because law was so openly manipulated by the

Communist Party during the Soviet period, to achieve policy goals, it is even more important that the post-Soviet Russian state adhere to the basic principle of equality before the law. While the situation has certainly improved, examples of insiders (both individuals and enterprises) being granted special exemptions remain commonplace. The sense that there are two standards—one for the ordinary citizen and another for the privileged elite—persists (though the composition of the elite has changed). Under such circumstances, building respect for law is dauntingly difficult.

### **Stimulating demand**

What might be done at this point in Russia's history to improve the image of law, and to make its use more palatable to its citizens? Is the answer more but better-drafted laws? Alternatively, is the answer better implementation of existing laws? Of course, both are important and need to be incorporated in any strategy. But the harsh reality is that there are no simple solutions. Still, a few guiding principles are worth stressing.

First, policymakers should shift their attention from supply to demand, in other words, from state to society. The laws and legal institutions should be reexamined from a bottom-up perspective. Providing remedies on paper is of little value if they are framed in obtuse legalese that is incomprehensible to nonlegal specialists or if they are ineffective. Policymakers need to think creatively about how to fashion remedies that are both appealing and realistic. For example, unpaid workers who sue their employers for back wages often discover, after "winning," that the sued enterprise has no liquid assets. The futility of their suit gives them little reason to view the law positively. Touting the existence of a remedy for wage arrears only makes state officials look out of touch and insensitive. Perhaps they need to be less ambitious. Perhaps the "rules of the game" for Russia in this time of transition need to be simpler and less sophisticated than those used elsewhere. After all, people will certainly not obey rules they cannot even understand or, if complied with, prove ineffectual.

This shift away from supply to demand will necessarily require a greater commitment on the part of the state to enforcement. But enforcement alone is not the answer. The resources required to run the courts

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and other legal institutions in a way that makes them usable are also essential. Moreover, rigorous-seeming implementing laws that do not “fit” into the existing legal culture are ultimately futile. All-important, on the other hand, is a commitment on the part of the state to obey the rules it imposes on others. Although professing publicly the ideals of the *pravovoe gosudarstvo*, the Russian government habitually exempts itself and its officials from the law. Self-exemption is most obvious in the arena of tax policy, where the state’s failure to pay its own debts has provided a convenient excuse for Russian enterprises not to pay their taxes. As one company official put it, “the government lies to us, so we lie to the government.” Whether this downward spiral can be halted—in the area of taxes or elsewhere—remains unclear.

Finally and most importantly, the appeal of law by itself cannot be assumed, either on an individual or societal level. Law’s potential to serve as a common

language, facilitating market transactions and easing democratization, has to be demonstrated, not assumed. This may require outreach efforts on the part of the Russian government, on both the national and regional levels, and a willingness to allow greater involvement of citizens and nongovernmental groups in the lawmaking process, in order to give them some sense of ownership—a stake—in the resulting legislation. Perhaps the motto of Russian legal reform should be changed to “seeing is believing.” Or perhaps the concept of private property, which ostensibly is the ultimate material incentive, should be applied to both the state and the law per se—it is “our” state, and the law belongs to us, too.

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