1995

Advising the Neocapitalists

James J. White
University of Michigan Law School, jjwhite@umich.edu

ADVISING THE NEO Captalists

— BY JAMES J. WHITE

IN THE EARLY 1920S, ANGELICA BALABANOFF, SECRETARY OF THE SOVIET COMINTERN, WROTE THAT ALL OF THE LEFT-WING WESTERNERS WHO HAD COME TO THE SOVIET UNION AFTER THE REVOLUTION OF 1917 FELL INTO ONE OF FOUR CATEGORIES: "SUPERFICIAL, NAIVE, AMBITIOUS OR VENAL." THE FALL OF COMMUNISM HAS BROUGHT A NEW GROUP OF WESTERNERS TO RUSSIA. UNLIKE THE VISITORS OF 1922 THESE ARE FROM THE RIGHT, NOT THE LEFT, BUT THEY MAY STILL FALL INTO COMRADE BALABANOFF'S FOUR CATEGORIES.

Professor White lectures a group of twenty-two Russian judges who visited the Law School last fall.

I AM ONE OF THE NEW RIGHT-WING VISITORS TO RUSSIA who have gone there to advise on drafting free market law, and I am not unique. Eastern Europe, Russia, and other countries that were formerly Soviet Republics are crawling with Western Europeans and Americans with advice about western commercial, constitutional, and other law. I write to reflect on what American lawyers can and will do for these emerging free market economies. I am more skeptical than most.

With the destruction of the Berlin Wall and the decline and ultimate dissolution of the Soviet Union, free enterprise has spread eastward across eastern Europe and into Asia, to Kazakhstan and beyond. China has seen a similar but more covert rise in capitalism. This rise of the free market has brought a call for free-market law. Laws on contract, sale of goods, negotiable instruments, mortgages, personal property security, and a variety of other things are needed of a kind never required in the controlled economies which formerly existed in Eastern Europe, the Soviet Union, and China.

Americans, British and Western Europeans have offered their laws as models. Organizations such as the American Bar Association, the United States Agency for International Development, and the Ford Foundation have held out helping hands to these countries. As an American expert on commercial law I have participated in these efforts. In 1993, Deborah Prutzman, a New York lawyer, and I spent a week in Beijing with Chinese drafters of the law on negotiable instruments. In a series of meetings since 1993 held in Ithaca, New York, and Moscow, Cornell University Law Professor Bob Summers and I have worked with the drafters of the Russian Civil Code. We worked under the auspices of the Institutional Reform and the Informal Sector program (IRIS) of the University of Maryland and at the invitation of one of its directors, David Fagelson, J.D. '85.

CHAUVINISM IS A PROBLEM, BUT THERE IS A FINE LINE BETWEEN ODIOUS CHAUVINISM AND APPROPRIATE FORCEFULNESS. FACED WITH CONSERVATIVE DRAFTERS WHO DO NOT FULLY EMBRACE THE FREE MARKET, ONE MAY NEED TO PUSH HARD TO ACCOMPLISH EVEN A LITTLE.

I write not to praise the work of Americans abroad but to note some of the difficulties I see for a "helper" who comes to a distant Asian or European country armed with experience about American law. While I have considerable optimism about the quality of law that will grow up in many of these societies, my work with the Russians and Chinese makes me skeptical about the benefits that Westerners provide.

Consider the barriers that face an American who would help another country revise its laws. A first problem is well known. It is the explosion that can occur when American chauvinism and arrogance is mixed with home country pride and defensiveness. It is a serious mistake to think the Chinese or Russians are ill informed about traditional law, and it is easy for an American commercial lawyer to exaggerate our law's influence on the success of our mercantile economy. (I suspect assertions about the influence of our law have it backward — in fact, our law is probably successful because of the mercantile economy and because of our stable and effective judicial system, not vice versa.)

Chauvinism is a problem, but there is a fine line between odious chauvinism and appropriate forcefulness. Faced with conservative drafters who do not fully embrace the free market, one may need to push hard to accomplish even a little. Home-grown drafters may simultaneously feel defensive about and superior to Americans — defensive because of the success of our commerce but superior

because of our ignorance of their language, laws, and history. I naively assumed that the Russians would base their new sales law on the United Nations Convention on the International Sale of Goods or on an American or Western European model. Not so; they started with the pre-Revolutionary Russian civil law! So the advisor must push — but not too hard.

A second challenge for a foreigner is to understand the experience, authority, and motivation of the local drafters. In Moscow, Bob Summers and I dealt with a committee that was composed mostly of people with professorial titles. Several members of the committee were also arbitrators or judges and some might be called research scholars. There were no business people, nor anyone who was or had been a private practitioner. In China, on the other hand, the committee was composed of professional drafters who worked for the legislature, but also of bankers from the central bank and from commercial banks. In both cases, I was impressed with the doctrinal knowledge of the legally trained persons.

The Russians reminded me of nineteenth-century American law professors; they had deep understanding of legal doctrine but no association with and limited concern for commercial transactions that were to be governed by the doctrine. For example, the Russians could easily hold their own on doctrinal debate on matters such as whether the perfect tender rule or the substantial performance rule should apply in performance of a sales contract. But they were not much interested in how that rule of law might affect the behavior of business people, nor were they much concerned with lawyers' manipulation of their rules. As Americans — deeply affected by legal realism — we instinctively ask: How will a lawyer attempt to manipulate this rule? To what transactions should this be applied? To what transactions will it be applied that I do not now contemplate? How might lawyers and business people modify their behavior in response to this law? Our Russian drafters might reply that those issues are not legal questions. Children of a communistic society and quite removed from commerce, the Russian drafters focus on doctrine. For them, it is business' job to conform.

A third problem for an American advisor is his ignorance of local business practice. For example, a large part of Articles 3 and 4 of the Uniform Commercial Code are devoted to the allocation of risk arising upon theft by check. Many of the most interesting American cases under those articles and much of what is taught in law school about them arise out of embezzlements in which corporate employees steal money by forging drawers' signatures, forging endorsements, and altering instruments. American experience is an artifact of the prevalence of checks in American commerce. We pay and get paid by checks; in most American companies, checks are everywhere. In Russia and China checks are rarely used. Detailed rules on allocation of risk from embezzlement by check are probably not necessary in those countries. Thus, Article 3 and Article 4 are not particularly good models for either of those societies.

Consider another example: it may make sense for the Russians to jump from a cash payment system directly to electronic payments and to bypass checks. The absence of roads, trucks and airplanes to carry checks around the Russian and Chinese countryside make paper transactions particularly unsuited for Russia and China.

Local conditions, such as persistently high inflation, may also intrude; inflation in Russia is a barrier to any system of speeded payments, electronic or otherwise. One of the reasons commonly given for the persistence of checks in the American economy is that drawers like the float conferred by the use of checks — float that is not available if payment is electronic and therefore nearly instantaneous.

The Russians know float. Not only private individuals and private banks enjoy float, but we were told that the central bank itself regards float as a source of income. Far be it for some foreign law professors to change Russian ideas about float if even the central bank lives on it. Thus, a law of the kind that the American Federal Reserve would indorse and support to reduce float by various methods is one that might be resisted by all but the purest idealist in Russia. So a big problem for an American advisor is ignorance of existing and emerging business practice and lack of appreciation of business actors' incentives and motivation.

Visiting Russian judges learned about juries by playing the role of one in a moot court session at the Law School.

These, of course, are obvious examples, but there are hundreds of others where the local practice differs from the American practice and where the law should differ too. Ignorant of those business practices and *a fortiori* ignorant of practice that is likely to develop coincidentally with the free market, an American has trouble advising a Russian or a Chinese.

A fourth problem in drafting abroad is the same here. It is often observed that someone who would influence a law that is being drafted by someone else is either too early or too late. When one comes with an earnest proposal for change in a draft, he is sometimes told he is too early: the drafter has not got to that part yet and it is not time to talk about it. When the earnest pleader returns five months or a year later, he may be told that the issue has been resolved and cannot be reopened. I have observed the problem — and even used the "early" or "late" excuse — as the reporter for the Revision of Article 5 of the Uniform Commercial Code.

That same problem exists abroad. For example, the Russians had done at least two drafts of Part One of the Civil Code before Bob Summers and I ever saw it in the fall of 1993. Apparently they had already redrafted Part One in conjunction with the Dutch in the summer of 1993. So most of our proposals were too late. As to Part Two of the Civil Code, he and I were too early in the fall of 1993. Part Two had not been written or at least was not yet ready for foreign critics.

A final problem for a foreign advisor arises from the nature of his relation to the advisees. Like a psychiatrist hired by parents to treat a reluctant child, the advisor is sponsored and paid by a foreign government or foundation. In all cases that I know of, the sending country pays the advisor; no fees are paid by the Chinese, the Russians, or other advisees. This means, of course, that advisors are guests, not employees. If advisors are not too troublesome, they may be nice to have around. But one gets his money's worth whether he listens to them or not, since he has paid nothing for the advice. I suspect that this is inevitable, but in Valhalla the host would pay and, having paid, would be more likely to listen.

In sum, I do not want to suggest that American lawyers' time and effort spent with the Russians, Eastern Europeans or Chinese has been wasted. I believe that some of the ideas that Bob Summers, Debbie Prutzman, and I have taken to them will be useful and will be incorporated in their laws. But it is far easier to exaggerate one's influence than to underestimate it. There are many good reasons why a foreigner's advice might be wrong or unhelpful and should command only one ear. There are also bad reasons why that will happen —- not the least of which are local sensitivity and chauvinism, and the inherent conservatism of the drafters and of the local parliament.

Believing that commercial law follows commerce, and not the reverse, I am not pessimistic about the state of law in China and Russia. Adverse tax or intellectual property laws may forestall foreign investment and a corrupt or ineffective judicial system may inhibit it, but I doubt that mediocre commercial law will seriously restrict investment. As commercial transactions grow and expand, I expect commercial law to accommodate to practice through legislative amendment, court decision and private law (such as arbitration). When business people seek "good" commercial law, they are not speaking as much about the substance of that law as about the stability and reliability of the judicial system.

Perhaps, of course, I am just confessing that commercial law is not too important, a dismal thought.

As Americans — deeply affected by legal realism — we instinctively ask: How will a lawyer attempt to manipulate this rule? To what transactions should this be applied? To what transactions will it be applied that I do not now contemplate? How might lawyers and business people modify their behavior in response to this law?

LQN

James J. White, J.D. '62, is the Robert A. Sullivan Professor of Law. He is the author of many books and articles on aspects of commercial law, including The Handbook of the Law Under the Uniform Commercial Code. *He also serves as the reporter for the revision of UCC Article 5.*

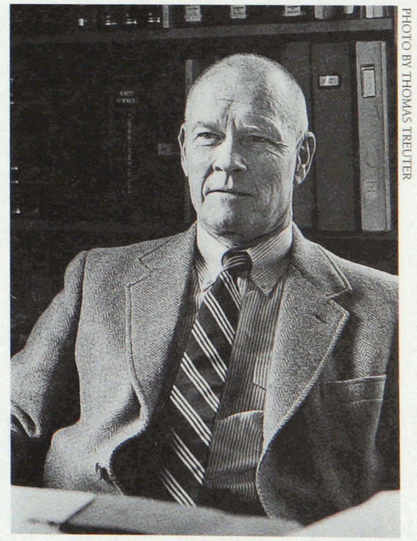

PHOTO BY THOMAS TREUTER