Review of Glinavos, I. (2010) Neoliberalism and the Law in Post Communist Transition: The Evolving Role of Law in Russia's Transition to Capitalism

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Ioannis Glinavos,

Neoliberalism and the Law in Post Communist Transition: The Evolving Role of Law in Russia's Transition to Capitalism

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The literature on the transition from central planning to "the" market in the former communist countries is dominated by economics and political science. In this book, Ioannis Glinavos both posits and objects that legal reforms are usually treated as an afterthought in the transition literature—although he more specifically finds his foes in the neoliberal, economic-transition literature, which he defines as a combination of Austrian economic thinking that views market individualism as the herald and prerequisite of individual freedom and neoclassical economic thinking that emphasizes the function of the market in promoting economic efficiency (p.19).

This is a strange marriage. Neoclassical thinking is concerned with general equilibrium and starts from the premise of an optimum, actually just as central planners did. Allocation of the factors of production then becomes a technical operation. Austrians reject the notion of such an optimum. To define and then to achieve an optimum would always require the use of force and would restrict freedom. In Austrian thinking, the market is an institution that allows individuals to engage in transactions, which they will do if it benefits them. For Glinavos, the combination of the two economic traditions allows for a perception of the state as rapacious and as in opposition to market; it is an organization catering to self-interested politicians and bureaucrats acting in order to benefit various client groups (p.19). However, the discussion of the state as an organization of self-interested politicians and bureaucrats can be well discussed within the framework of neoclassical thinking. These individuals are merely optimizing their individual utility functions, which subsequently obstructs the social optimum. Bureaucracies simply are inefficient; there is no need for Austrian thinking in this approach.

Glinavos brings in Austrian thinking because of its explicit discussion of the role of law. One of the foremost Austrian thinkers, Nobel-prize winner Friedrich Hayek, distinguished an essential procedural conception of the rule of law—requiring the neutral application by an independent judiciary—from a more substantive one where the rule of law requires certain things of content of the legal rules themselves, more specifically, the state should confine itself to establishing rules applying to general types of situations and should allow the individual freedom in everything that depends on the circumstances of time and place.

Neoliberal thinking—with its focus on the protection of private property rights and the ensurance of contractual obligation as the most important role for law—matches this restricted substantive Hayekian meaning very well. Glinavos subsequently argues that neoliberals have too narrow an interpretation of the rule of law and, furthermore, that the promotion of the rule of law is rather different from wider institutional reform. He presents two major arguments. *First*, he points out that concept of the rule of law is overused and ideologically abused and, therefore, has lost meaning. The ideological abuse pertains to the perception that law is an objective system to resolve disputes and is without distributional elements, which contrasts to the *ad hoc* decision making power of politicians. However, law creates 'rights-obligations structures', and thus law creation is an inherently political process; creating a legitimate legal system, therefore, necessitates political credentials (p.157). He further points out that in societies with widespread poverty and extreme inequalities of wealth, redistribution may well be a desirable part of a reform program that aspires to acceptance and legitimacy. *Second*, with respect to institutional reforms, the author builds on the work of another Nobel laureate, Douglas North, as one of the founders of the new institutional economics to point to the extension of formal rules (laws, constitutions, rules) to informal constraints (conventions, codes of conduct, norms of behavior) and effective enforcement to argue that institutions matter for development (p.111).

Some neoliberal authors, indeed, acknowledge the importance of institutions and accept that to protect property and safeguard transactions there is a need for a strong government. But since such a government then also is able to expropriate, there is a need to constrain state power by an independent parliament, independent judiciary and other institutions. Glinavos labels this a narrow interpretation of the importance of institutions, which stays within the confinements of neoliberal thinking. He points out that neoliberal theory assumes the existence of an independent, neutral apolitical economic rationality. Markets are not politically or legally constituted but, rather, rooted in human nature; they are purely economic and apolitical. As long as private property rights are protected and contracts are honored, any distribution of ownership rights will lead—via the market—to efficient use of the means of production. This helps advocates of economic reform to dismiss the specific circumstances of a country in transition. According to Glinavos, the basic neoliberal assumptions are wrong as markets cannot be described as self-regulating when they require the sort of institutional supports for which the new institutional economists argue. The rigid division between politics, law and economics lead to the erosion of trust in the institutions of capitalism.

The author—who is City Solicitors' Educational Trust Lecturer in Contract Law at Kingston University in the UK—prefers a broader interpretation where there are more interdependencies between respect for the law, neutral enforcement of rules and other defining elements of the rule of law as forming the abstract elements and the market supporting institutions as the specific elements of post-communist reforms. In the marrying of economics, social interaction and politics through market supporting institutions, a demand for the rule emerges. Outcomes that are a product of playing by the rules will also be seen as legitimate (p. 113).

Glinavos presents a theoretical, foremost critical, evaluation of the neoliberal position; but, to challenge its dismissal of specific circumstances, he uses the developments in Russia in the 1990s. In my view, this is the weakest link in the book. It is true that the World Bank—and even more so its sister organization the International Monetary Fund—were involved in providing advice to Russia and, also, that this advice ran along the lines of the narrow interpretation of institutional economics. However, Glinavos does not convincingly argue that developments in Russia shaped the position of these organizations; nor does he convince this reader that developments in Russia prove the neoliberals have been wrong. I will be brief on the first issue since that is not the central topic in this book; but it is obvious that the international organizations have worked in close collaboration with the successive Russian governments and have taken political developments into consideration to maintain legitimacy in Russia.

With respect to the criticism on the neoliberal economic thinking, Glinavos would have been more convincing if he had approached his topic from another angle. He argues that Russia was subject to a policy of ‘instant capitalism’ that was taken from the book of neoliberal theories and ascribes the lack of progress in Russia as a result of that. But developments in Russia in the early 1990s were a far cry from the preferred policies of neoliberals.

Towards the end of the Soviet Union in the fall of 1991, Russian reformers and their western advisors were convinced of the need for a fast and fundamental break with the past to upset the stronghold of the Communist Party on economic and political life and for shock therapy to immediately liberalize prices, reduce state deficits and taxes, and privatize state-owned-enterprises. (This is close to what ‘instant capitalism’ as advocated by neoliberalism proposes.) This suited the political agenda of ‘reform’ president Boris El’tsin very well, and he therefore initially supported the reform agenda. But he objected to the liberalization of energy prices for instance, which had far reaching effects in subsequent developments. However, since Russia’s reformers were more concerned about rolling back the state and they did use the term ‘to depoliticize’, El’tsin—later in 1992—dismissed his reform-minded Deputy Prime Minister Egor Gaidar without further ado to pacify the political opposition against the reforms in the Russian Supreme Soviet, the Russian parliament.

There also were altercations with respect to the privatization of enterprises. Privatization was one of the major intended reforms; this, of course, requires a change in the legal system, among others the protection of private property. The reformers wanted fast privatization and preferred to give away the enterprises to the population through a voucher system where every citizen would receive a voucher with which s/he could bid on enterprises. Again, parliament, pressed by the existing enterprise directors, protested; as a result, a compromise was reached where voucher privatization was available for a minority share in enterprises only. Some enterprises were deemed strategic and excluded from privatization entirely, while others managed to circumvent the loss of control by creating new enterprises.

Ultimately, Russian privatization—in the first half of the 1990s—was a rather opaque and highly politicized process. The link between politics and economic interests became even clearer in the so-called ‘loans-for-shares’ program of 1995/1996 in which entrepreneurs with close contacts to the president were able to gain ownership of valuable firms in the resource extracting industries mainly. But here too, parliament was able to obstruct the plans and to limit the number of enterprises that were thus privatized. In fact, there has never been a rigid division among politics, law and economics in Russia, and there is ample evidence that the lack of political support and legitimacy and the arrogance of reformers towards the opponents of their agenda are major causes for the failure of ‘shock therapy’.

This would change the argument of Glinavos somewhat; from ‘reforms result in the lack of political legitimacy’ to ‘it is impossible to reform without political legitimacy’, but its core would remains intact, *i.e.*, the neoliberal approach to ignore politics and law is illusionary.

An important argument for Glinavos is that income- and wealth distribution have to be part of a reform policy to gain acceptance and legitimacy. The Russian reformers who advocated shock therapy but who compromised on voucher privatization argued that, ultimately, it did not matter how privatization was achieved as long as it was achieved, since the new owners would surely reform their business to increase efficiency and to turn a decent profit.

This failed to happen and income in Russia declined during most of the 1990s. The population became disappointed in the reforms, and the outcome of the privatization drive was a particular source of disillusion. It has to be noted, however, that the lack of legitimacy for the reform policies was caused by the haphazard rule and ensuing political chaos in the El’tsin era as much as by the unfair outcome of the reforms. It made it easier for El’tsin’s successor Vladimir Putin to strengthen, once again, the state in both politics and in economic affairs. In the most outlandish case of the reversal of ownership, the Yukos case, Michael Khodorkovskii lost ownership of this company. Neoliberal reformers had praised Khodorkovskii for having turned the company around and saw this as a justification of their ‘it does not matter how you privatize’ case; yet, the oil tycoon could not count on any popular support for his cause.

Developments in Russia do pose other problems for Glinavos’ argument. Putin’s legitimacy, for instance, is not necessarily democratic. His policies fit in a Russian tradition of highly centralized power where political authorities rule *de facto* or *de jure*. This may even result in a more efficient economy in Russia, in which case—to return to the definition of neoliberalism—neoclassical thinkers may mark his regime as an improvement to the current situation. Austrian thinkers, however, like Glinavos, are more concerned with the legitimacy of these outcomes. On principal grounds, a market economy for them is more democratic than political decision making since people can freely engage in transactions. With neoclassical thinkers, they share the relative silence on distributive effects. Glinavos advocates democracy but does not subject democracy to the same scrutiny as he does the market economy and its supporting institutions. Why, for instance, would 'voting' with rubles be any less democratic than voting through the ballot or through other ways of representation? Here too, one of the most important issues would be income- and wealth distribution.

The author has written a passionate critique on neoliberalism, and his analysis on the treatment of the rule of law in the discussions on reform—in Russia and elsewhere—are well worth reading; his conclusions that one cannot dismiss politics and law from economic policy, and that distribution issues matter, are convincing. His discussion of Russia itself could have contributed more to his conclusions had he not assumed that a neoliberal policy actually was implemented there, because it was not.

Russia's transition was a very political affair, and the most ardent neoliberals actually argue that that caused the poor results in Russia's reforms. The weakest link in the book is, indeed, Glinavos' discussion of Russia since he credits neoliberalism for most maladies in the country. That is not fair to neoliberalism, nor does it do justice to the developments in Russia. Also, the reformers in Russia and their advisors were typical representatives of neoclassical, not Austrian thinking; therefore, from a Russian perspective, it becomes puzzling why the definition of neoliberalism marries neoclassical thought with ideas of the Austrian school.

It is of course difficult to take the developments of a specific country and use these to enter a more theoretical discourse; but somewhat more reservation would, therefore, have been appropriate.

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Joop de Kort holds a Ph.D. from Tilburg University, The Netherlands; the subject of his dissertation was on the failure of central planning. He works in the field of transition economics, with a special interest in the relationship of Russia with its “near” (CIS) and its “far abroad”. He has published on topics such as entrepreneurship; more specifically, on Dutch direct investments in Hungary, and developments in the Russian aviation sector (with Steven Kluiters). More recently, his work has focused on Russia’s membership in both the IMF and the WTO. Dr. de Kort has held positions at the Universities of Tilburg and Groningen, The Netherlands, before coming to Leiden in 1998 to teach international economics and Russian economic transition.