

Judicial Systems in Transition Economies

Assessing the Past,
Looking to the Future

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THE WORLD BANK
Washington, D.C.

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1 2 3 4 08 07 06 05

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ISBN-10: 0-8213-6189-9 ISBN-13: 978-0-8213-6189-4

eISBN: 0-8213-6190-2

DOI: 10.1596/978-0-8213-6189-4

Cover design by Naylor Design, Inc.

Cover photos of the Armenian courtroom and building: Eric N. Peterson; other photos: World Bank.

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Acknowledgments

This study was prepared by the Poverty Reduction and Economic Management Department (ECSPE) in the Europe and Central Asia (ECA) Region. It was written by James Anderson, David Bernstein, and Cheryl Gray. Erlinda Inglis provided expert assistance in the preparation of this study. The authors would like to thank Erica Westenberg for research support and preparation of appendix 1, and Luba Beardsley and Friedrich Peloschek for input to chapter 2 and appendix 2, respectively. Peer reviewers were Donna Dowsett-Coirolo, David Freestone, Waleed Malik, and Andrew Vorkink. The authors would also like to thank Frances Allen, Gerhard Botha, Klaus Decker, Hans Jurgen Gruss, Kathy Lalazarian, Brian Levy, Rick Messick, Pradeep Mitra, Stefka Slavova, Debbie Wetzel, and other members of ECA's Thematic Group on Legal and Judicial Reform for their specific comments on the draft and/or their inputs into the Bank's strategy and operational approaches in this area of work.

Acronyms and Abbreviations

| | |
|-----------|--|
| ABA–CEELI | American Bar Association–Central European and Eurasian Law Initiative |
| ADR | alternative dispute resolution |
| ALB | Albania |
| ARM | Armenia |
| AZE | Azerbaijan |
| BEEPS | Business Environment and Enterprise Performance Survey |
| BEL | Belarus |
| BiH | Bosnia and Herzegovina |
| BUL | Bulgaria |
| CEE | Central and Eastern Europe |
| CIS | Commonwealth of Independent States |
| COE | Council of Europe |
| CRO | Croatia |
| CSO | civil society organization |
| CZE | Czech Republic |
| EBRD | European Bank for Reconstruction and Development |
| EC | European Commission |
| ECHR | European Court of Human Rights |
| ECSPE | Europe and Central Asia Poverty Reduction and Economic Management Department |
| EOS | Executive Opinion Survey |
| EST | Estonia |
| ESW | economic and sector work |
| EU | European Union |
| FRY | Federal Republic of Yugoslavia (now Serbia and Montenegro) |
| FYR | former Yugoslav Republic (of Macedonia) |
| GDP | gross domestic product |
| GEO | Georgia |
| HUN | Hungary |

ACRONYMS AND ABBREVIATIONS

| | |
|------|---|
| IDF | Institutional Development Fund |
| IFI | international financial institution |
| IMF | International Monetary Fund |
| IT | information technology |
| JRI | Judicial Reform Index |
| KAZ | Kazakhstan |
| KYR | Kyrgyz Republic |
| LAT | Latvia |
| LIS | Legal Indicator Survey |
| LIT | Lithuania |
| MAC | FYR of Macedonia |
| MOL | Moldova |
| NGO | nongovernmental organization |
| OECD | Organisation for Economic Co-operation and Development |
| PAL | Programmatic Adjustment Loan |
| POL | Poland |
| ROM | Romania |
| RUS | Russian Federation |
| SAM | Serbia and Montenegro |
| SEE | Southeastern Europe |
| SLK | Slovak Republic |
| SLN | Slovenia |
| SSA | Sub-Saharan Africa |
| TAJ | Tajikistan |
| UKR | Ukraine |
| UN | United Nations |
| UZB | Uzbekistan |
| WVS | World Values Survey |

Note: All monetary amounts are in U.S. dollars unless otherwise indicated.

Executive Summary

WELL-FUNCTIONING LEGAL AND JUDICIAL INSTITUTIONS ARE CRITICAL to economic growth and poverty reduction in market economies. They define the rules by which markets function, and they provide a means to resolve disputes, protect economic and social rights, and hold governments accountable for their actions. The transition from socialism to capitalism in Central and Eastern Europe and the Baltics (CEE) and the Commonwealth of Independent States (CIS) has required a fundamental reorientation of legal and judicial institutions. During socialist times they were subordinate to the executive and the Communist Party, and their role in the commercial sphere was oriented almost entirely toward enforcing the governments' economic plans. The scope for private transactions and private law was narrow. Administrative law and institutions—including state arbitration—represented the most extensive part of the legal infrastructure. The transition from socialism to capitalism requires a dramatic change in legal and judicial institutions: heightened independence from the executive; new roles and skills for judges, lawyers, and other personnel; and a rapid increase in institutional capacity to handle legal cases efficiently and effectively.

This study looks at the experience of the CEE and CIS transition economies in their efforts to reform their legal and judicial institutions to fit the needs of a market economy. It draws on numerous sources of data—including the European Bank for Reconstruction and Development (EBRD)–World Bank *Business Environment and Enterprise Performance Surveys*, the American Bar Association–Central European and Eurasian Law Initiative (ABA–CEELI) *Judicial Reform Index*, the EBRD *Legal Indicator Survey*, the World Bank's *Doing Business* database, the *World Values Survey*, the World Economic Forum's *Global Competitiveness Reports*, and the *New Democracies and New Russia Barometer* surveys conducted by the University of Strathclyde—to measure specific characteristics of legal systems in various transition countries and how they have changed in recent years, and to draw lessons for future reforms.

Experience in the 1990s

The CEE and CIS countries faced a monumental transition challenge at the beginning of the 1990s. It is perhaps not surprising that domestic reformers and much of the international community initially emphasized political transformation, macroeconomic stabilization, and basic structural reforms (including privatization) over longer-term institution-building needs. In this hectic environment, the creation or strengthening of legal and judicial institutions took a back seat to passing laws and decrees to support and implement macroeconomic and structural reforms. The European Union (EU) accession process, with its focus on adopting the *acquis communautaire*, was also a major driver of lawmaking in Central and Eastern Europe. In most countries, less attention was paid to transparency or broad participation in the lawmaking process. Efforts to solicit input or feedback from enterprises, lawyers, or judges who would use, interpret, or be affected by proposed laws were minimal.

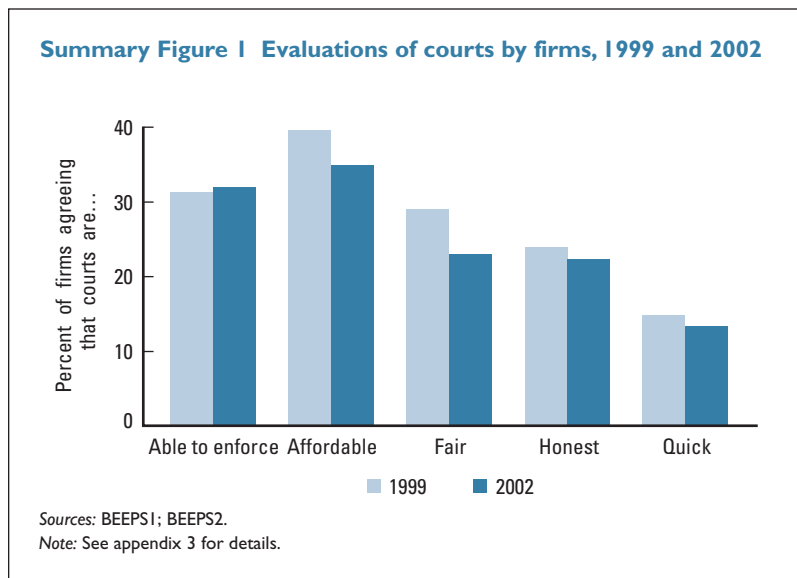
As a result of weak capacity and rapid and nontransparent lawmaking processes, existing institutions—including courts, lawyers, regulatory bodies, and others charged with implementation—often had difficulty understanding, applying, and enforcing the new laws being passed by Parliaments. This led to significant “implementation gaps”—that is, gaps between what legislation required and what happened in practice, which in turn led to growing public mistrust in courts. Throughout the 1990s, less than half of the citizenry in transition countries where they were surveyed said that they trusted the courts, and this level of trust tended to decline over the course of the decade. However, other institutions of state tended to be even more beset by lack of trust. The first decade of transition closed with a reduced role for the state in the incipient market economy, juxtaposed with a widely held view that state institutions were too weak to be effective.

Some early judicial reforms were undertaken, supported in many cases by donor assistance. They tended to focus on creating an independent and depoliticized judiciary, free from state control, which could act as a bulwark for newly won political and civil rights. In addition to drafting and adopting constitutions that enshrined the idea of an independent judiciary, efforts to promote judicial independence focused on certain formal aspects of the judicial system, such as the appointment, tenure, removal, and disciplinary procedures for judges; the development of self-governing bodies for the judiciary; and the creation of judge-controlled

training institutes. The transition countries also created new, specialized constitutional courts staffed with new judges (mainly scholars and academics) to hold governments accountable and institutionalize the protection of civil and political rights. More detailed procedural and organizational changes that could make the courts work “better” by making them more efficient and accessible were usually not included in the early judicial reform efforts.

Status at the start of the 21st century

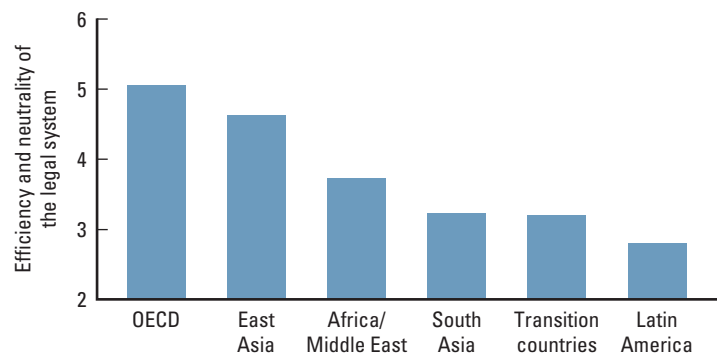
The data sources noted above provide an in-depth snapshot of the state of legal and judicial institutions in transition countries at the beginning of the 21st century, approximately 10 to 12 years into transition. They clearly show the primacy given in the 1990s to establishing judicial independence over ensuring efficiency and accountability. While the data indicate that there is still some way to go in establishing independence, there is much further to go in creating courts that are quick, affordable, effective, fair, and honest (summary figure 1). Citizens and firms in most countries see courts as slow and expensive, and data on the time required to collect a debt through the courts reinforces this view. Only about one-quarter of 6,000 firms surveyed in 26 transition countries in 2002 viewed



the courts as fair or honest. Surveys of firms and of the general public about corruption often identify the courts as among the entities perceived to be the most corrupt, although there is some evidence that actual bribes to the courts may have decreased slightly in the region as a whole between 1999 and 2002. Finally, less than 40 percent of the firms surveyed in 2002 viewed the courts as able to enforce their decisions. Not only are firms' and citizens' views of courts generally negative, but also they appear to have worsened rather than improved (at least until 2002) along critical dimensions in the majority of transition countries (including several that recently entered the European Union). Indeed, it is probably fair to say that less overall progress has been made in judicial reform and strengthening than in almost any other area of policy or institutional reform in transition countries since 1990. Furthermore, firms' perceptions of the legal and judicial systems in transition countries are worse than comparable perceptions in most other regions of the world, according to a recent worldwide survey of business executives (summary figure 2).

Many dimensions of court performance matter for doing business. Firms want courts that are fair and honest, strong enough to enforce their decisions, fast, and affordable. Yet reforms that might strengthen one dimension—such as independence—may weaken another—such as

Summary Figure 2 Perceptions of the efficiency and neutrality of the legal system, 2004



Source: World Economic Forum, Global Competitiveness Report 2004.

Note: See appendix 3 for details. OECD = Organisation for Economic Co-operation and Development. Transition countries that are currently OECD members are grouped with transition countries for this chart. (1 = inefficient and subject to manipulation...7 = efficient and follows a clear and neutral process.)

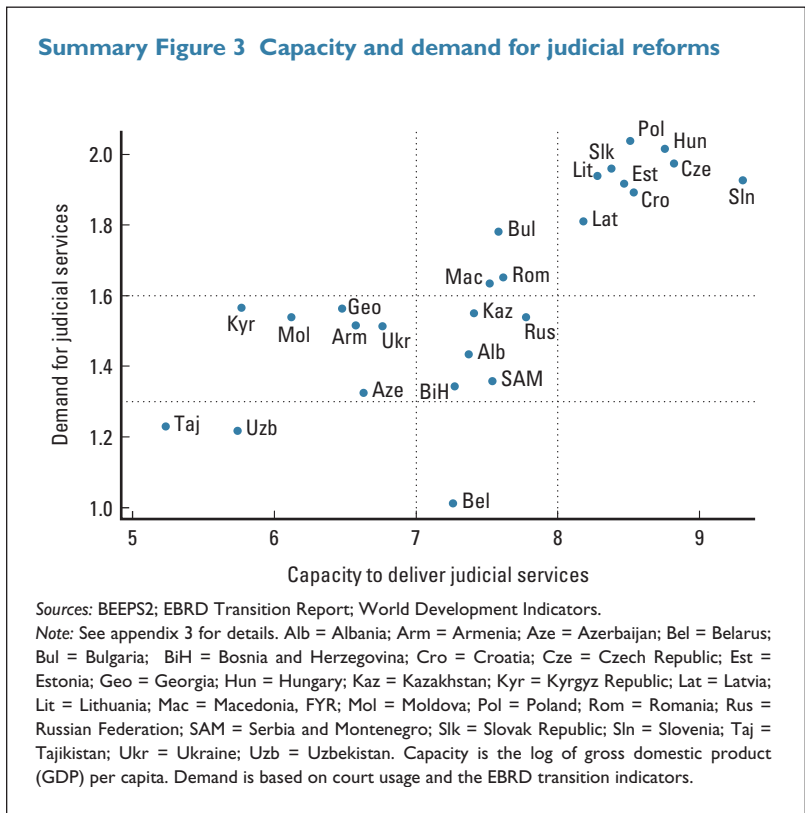
accountability, at least in the short run. Furthermore, it is clear that the transition process has led to an explosion in the number of legal cases, and in countries where firms use courts more extensively, firms are less likely to rate their courts as “quick.” Thus there is a complex relationship between use and perception of the courts, with greater reliance on courts (even if useful) not necessarily leading to better perceptions. Clearly the reform of legal and judicial institutions is a long and complex process that will continue to require dedication and patience.

The reform agenda

Countries and donors are now placing increasing emphasis on the need to improve the structural and operational independence, efficiency, accountability, and enforcement capacity of judicial institutions. Since 1997 the European Commission (EC) has pointed to weaknesses in the implementation of laws, particularly the lack of capacity and other problems in the judiciary, as key constraints in the accession process, and it has encouraged candidate countries to use its accession assistance to address these institutional constraints. The World Bank and other donors are also putting more resources toward increasing the efficiency and effectiveness of legal institutions, including supporting the introduction of modern facilities, case management practices, information sharing, training of judges and other court personnel, and stronger mechanisms to ensure transparency and accountability.

While general lessons can be drawn from the analysis about the range of reforms that might be needed, not all issues are of immediate relevance to every transition country. Transition countries differ significantly among themselves, not only in the specific problems they face but also in both judicial capacity and in the “demand” for well-functioning judiciaries. Both demand and capacity are in turn related to the extent of economic reform and the per capita income in the country concerned. Summary figure 3 places transition countries along these two dimensions of judicial capacity and societal demand for business-related judicial services. In large part, the strategy and priorities for each country going forward will depend on what its particular problems are and where it lies in this typology.

In countries where businesses’ demand for well-functioning judiciaries is relatively weak because market reforms have been shallow, the



priority is to build basic demand for impartial dispute resolution through continued market reforms. As a private sector and enhanced demand for judicial services emerge, increased emphasis can be placed on the courts themselves—to building greater accountability and independence while gradually strengthening their capacity.

Countries that are further along on the economic reform path face a more complex challenge. The demand for judicial reforms has strengthened, which both puts the spotlight on problems of judicial capacity and suggests that further reforms and capacity building are worth the effort and may be sustainable. In this situation the question of priorities and sequencing is often center stage. If capacity is relatively weak, top priorities for action are likely to include continued structural reforms—including efforts to enhance independence and accountability—and basic investment in capacity, such as testing of judges to ensure competence, refurbishing selected court buildings to provide functional space, providing simple

information technology (IT) infrastructure to allow information sharing, and financing the hiring of clerks or administrators to free-up the time of judges. If capacity is somewhat stronger, judicial strategies may focus on more complex aspects of court performance. The moderate demand for reforms, however, does not guarantee against backsliding, and continued attention to market reforms should still play an important role in such environments.

The opportunities for judicial strengthening are greatest (and perhaps counter-intuitively, the levels of public dissatisfaction likely to be highest) where demand from the business community is strong. Comprehensive judicial reform strategies addressing all aspects of reform— independence, accountability, court efficiency and performance, access and affordability, alternative dispute resolution mechanisms, and the design and functioning of related professions (such as the bar, bailiffs, and notaries)—may be appropriate in these settings. If capacity is already relatively high, as in the new EU member states, reforms can be less comprehensive and focus more on remaining areas of weakness.

As this study suggests, there is much work to be done. The efficient functioning of legal and judicial institutions is an urgent priority that deserves our focused attention.

1

Introduction

LEGAL AND JUDICIAL INSTITUTIONS PLAY A CENTRAL ROLE IN THE functioning of market economies. In working to define and enforce laws, resolve disputes among private parties or between citizens and the state, and oversee and counterbalance the power of the executive, they help to define the investment climate in which firms operate and the legal setting in which social and human rights take shape. Literature on economic development and socialist transition over the past decade has increasingly stressed the critical importance of well-functioning institutions to economic growth, social development, and poverty reduction.¹ While legal and judicial institutions can vary markedly among countries in their structure, functions, and degree of formality, they must be seen as legitimate and relied upon by the citizenry if they are to play an effective role in an economy and society.

One of the most momentous developments in recent world history was the end of socialism in Central and Eastern Europe (CEE) and the breakup of the former Soviet Union into independent states (most of which are loosely joined in the Commonwealth of Independent States, or CIS) at the beginning of the 1990s. The transition from socialism to market economies in this part of the world over the past 15 years has required a radical reorientation in economic and social policies and a complete rebuilding—or often building from scratch—of core institutions. Among the biggest challenges has been the reorientation or recreation of legal and judicial institutions, which in the early 1990s were ill suited to the needs of a market economy. They faced a myriad of fundamental challenges, including establishing independence from the executive, developing new means to ensure accountability given such newfound independence, creating new management tools and approaches, ensuring greater transparency and sharing of information, and building new competencies for judges and other legal personnel.

The goal of this study is to analyze progress to date in the reform of legal and judicial institutions in the transition countries of CEE and the CIS. It draws together information and data from various expert assessments and surveys of firms, lawyers, and the population to paint a picture of where the process started in 1990 and how it proceeded through the 1990s (chapter 2), where it stood 10 to 12 years into the process at the start of the 21st century (chapter 3), and what lessons might be drawn for the future (chapter 4). Box 1.1 provides a brief description of data sources used in the analysis.

Box 1.1 Sources

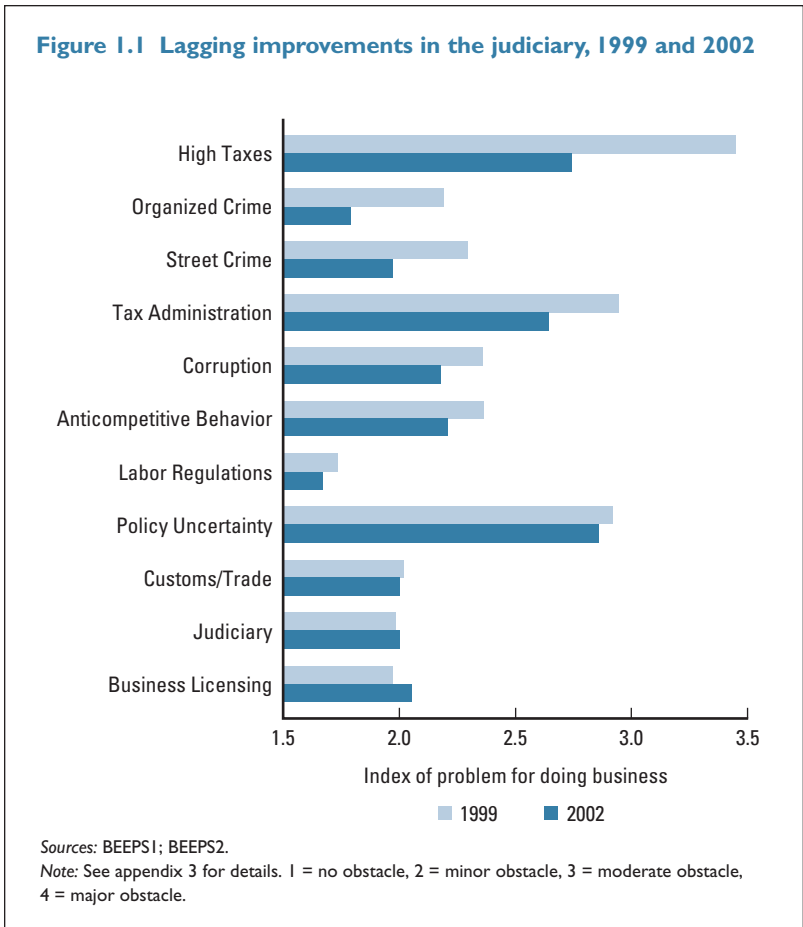
This paper draws on many data sources on the ways that firms interact with the legal and judicial systems and on the qualities of those systems. The data sources include subjective assessments by experts and data from surveys of firms, lawyers, and the general population. The primary sources include:

- The *EBRD-World Bank Business Environment and Enterprise Performance Survey* (BEEPS) was undertaken in two rounds in 1999 and 2002. The surveys covered more than 10,000 firms in Europe and Central Asia. More information is available at: <http://www.worldbank.org/eca/governance/>.
- The *ABA-CEELI Judicial Reform Index* (JRI) consists of subjective indications of how characteristics of a country's judicial system correspond with certain principles of good judiciaries. The JRIs have been constructed one country at a time since 2001. The JRI indicators are not numerical and, indeed, the authors explicitly stated that they wanted to avoid "ranking" countries. For the purposes of this paper, numerical scores were assigned. See appendix 3 for details. More information is available at: <http://www.abanet.org/ceeli/publications/jri/home.html>.
- The *EBRD Legal Indicator Survey* (LIS) is a survey of major law firms in transition countries about the legal systems in those countries. The LIS has been conducted annually since 1997. The aggregates obtained from the LIS form the basis of the *EBRD Legal Transition Indicators*. While the LIS is characterized as a perception-based survey of practicing lawyers, in some countries its results are better viewed as expert assessments, given the small sample size. More information is available at: <http://www.ebrd.com/country/sector/law/about/assess/main.htm>.
- The World Bank *Doing Business* database includes indicators constructed from a broad range of sources. The indicators used in this paper are based on surveys of lawyers in 2003 and 2004. More information is available at: <http://rru.worldbank.org/doingbusiness/default.aspx>.
- The *World Values Survey* has been conducted for decades and includes 13 transition countries and jurisdictions in 1990, providing a useful snapshot of trust and attitudes toward the role of the state at the beginning of transition. Further information is available at: <http://wvs.isr.umich.edu/index.shtml>.
- The *Executive Opinion Survey*, conducted by the World Economic Forum and published in its *Global Competitiveness Reports*, includes many questions on how business managers view the legal system. This study uses data from the 1998 through 2003/4 issues. Further information is available at: <http://www.weforum.org/>.
- The Centre for the Study of Public Policy at the University of Strathclyde has conducted numerous public opinion surveys in transition countries since the early 1990s and these are published as the *New Democracies Barometer* and *New Russia Barometer*. The questions on trust in various institutions, including the courts, are of relevance here. Further information is available at: <http://www.csp.strath.ac.uk/>.

The study focuses primarily on judges and courts, although it recognizes that the universe of legal institutions includes a wider range of institutions,² and some of the variables included in the analysis look at the efficacy of the system as a whole. Appendix 3 provides greater detail on the variables used, and appendices 1 and 2 provide a comparative look at similar issues in Turkey and brief summaries of the World Bank's activities in support of legal and judicial reform in transition countries.

While this study is the first to take a comprehensive look at available data on the legal and judicial systems of transition countries, the data sources are not comprehensive. As noted in box 1.1, the surveys involve primarily commercial and business interests, and most do not address how other social or economic groups view the judicial system in these countries. The surveys vary in coverage and methodology, with some being oriented more toward measuring broad public perceptions and others attempting to analyze actual experiences of firms and citizens in using the courts.³ In addition, some of the data sources are limited in time; both the *EBRD–World Bank Business Environment and Enterprise Performance Survey* (BEEPS) and the EBRD's *Legal Indicator Survey* provide data only through 2002 and thus do not capture legal and judicial reforms that may have occurred since that time, particularly in countries that undertook significant reforms prior to joining the EU on May 1, 2004.⁴

The transition years have been extremely difficult for the countries concerned, with many political and economic hurdles and ups and downs in economic growth and stability. To put the issue of legal and judicial reform in this region in broader perspective, it is interesting to see how firms in CEE and the CIS view the functioning of the judiciary compared to other challenges they face in doing business. The data in figure 1.1 are drawn from the *EBRD–World Bank Business Environment and Enterprise Performance Survey*, a survey of 4,500 and 6,000 firms, respectively, conducted in 1999 and again in 2002 across the region. Two findings are evident in figure 1.1. First, while many firms consider the functioning of the judiciary to be a problem for their business, they are even more critical of several other aspects of the business environment—most notably taxes and corruption. Second, however, these other more problematic aspects of the business environment appear to have improved between 1999 and 2002, while firms discern no noticeable improvement in the functioning of the judiciary. Indeed, as will be illustrated below, most indicators for the judiciary seem to be getting worse in many transition countries. As the countries advance and firms rely even more on the



formal legal system to handle business disputes, the pressure on courts will only increase. Strengthening legal institutions is a central challenge of the next decade.

Notes

1. For a discussion of the role of legal and other institutions in economic development, see North 1990; Bardhan 1997; Williamson 1985; World Bank 1996; World Bank 2002; World Bank 2004a. For a collection of empirical essays on the use of law, see Murrell, ed., 2001.
2. The universe of entities that can fit within a broad definition of legal and judicial institutions is very large—including not only courts and judges,

but also police, lawyers, prosecutors, bailiffs, arbitrators, mediators, and company and property registers, as well as other more focused regulatory or administrative bodies charged with setting and enforcing legal and regulatory norms.

3. Studies have shown that the general public's opinions of courts may be slow to change, while targeted surveys aimed at those with recent experience in the courts are likely to provide a better measure of changes in court performance. See Toharia 1994; Kritzer and Voelker 1998.
4. Among transition countries analyzed in this study, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, the Slovak Republic, and Slovenia joined the EU in May 2004.

2

The First Decade of Reform

Antecedents

The former socialist countries of Central and Eastern Europe and the former Soviet Union began the transition process in the early 1990s with public institutions that were ill suited to the needs of a market economy. Legal and judicial institutions were no exception. While legal systems in socialist economies may have looked on the surface similar to those in Western market economies—with, among other things, an extensive network and reliance on courts, lawyers, and prosecutors—the roles of both the system itself and the actors within it were very different from analogous roles in market economies. According to socialist theory, the socialist state was the instrument through which a classless society would be created, and the socialist state itself was to be ruled by a majority working class. Thus, the governance structure, including the judiciary, was designed to enforce the interests of the working class, as represented by the communist party. The ideas of separation of powers, a limited state, and individual rights vis-à-vis the state were essentially absent from this worldview.

Socialist law

In the socialist state, public law¹—especially administrative and criminal law—and the institutions to enforce it dominated the legal system. Administrative law² regulated the actions of administrative agencies of the government. Since the socialist state assumed a dominant role in managing both the economy and social life, administrative law and

institutions—which were part of the executive branch—represented the most extensive part of the legal infrastructure. The legislative process relied heavily on sub-laws and regulations that interpreted and applied the primary legislation.

The content of socialist laws was also designed to achieve the aims of the socialist economic system. Criminal laws and institutions sided with the interests of the “working class”—in practice the communist party. Special “crimes,” such as the prohibition against entrepreneurship, protected the state economic monopoly. The prohibition against “parasitism” enforced full employment. Attacks against state ownership were punished by more severe sanctions than attacks against private or personal ownership, and people belonging to the working class even received lesser punishments in certain cases.

Given the broad coverage of public law, few issues were left for the field of private law.³ Most private law covered family matters and the limited number of economic transactions allowed among individuals (such as the transfer of houses). Socialist laws governing private transactions in CEE and the CIS were based on civil law principles with modifications to enforce Marxist-Leninist ideology. Prior to socialism these countries had long legal traditions based on Roman civil law, and socialist principles were essentially grafted on to this civil law base. This actually eased the later transition away from socialism somewhat, by giving some transition countries a more advanced starting point from which to adapt their legal system to the needs of a market economy.⁴

Socialist legal institutions

Legal institutions functioned no differently from other government agencies: they focused on managing the economy and engineering society in ways that would be consistent with overall ideological objectives. As the economy was centrally planned and managed, most economic agents in the market were state-owned companies. Enforcement of contracts and property rights among these economic agents was seen as the job of the state and its administration and was generally handled by a special agency—state arbitration, usually controlled by the Ministry of Economy—rather than the courts. Arbitrators were not supposed to be independent, and the primary objective of these proceedings was fulfillment of the state economic plan rather than justice per se. The outcome

was determined with reference to the needs of the economic plan or by negotiations among top managers. The organization, working procedures, human resources, budget, and information and asset management of state arbitration all reflected its underlying role and purpose in this centrally planned regime.

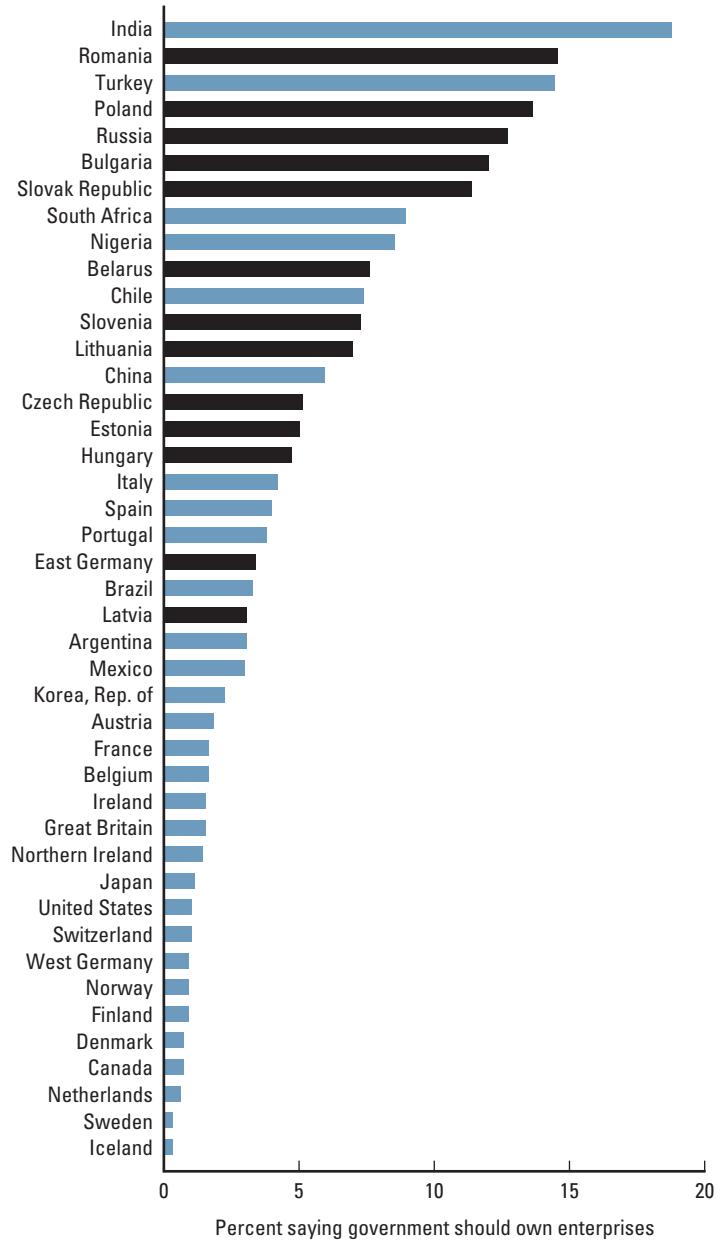
The judiciary, in contrast, was responsible primarily for noneconomic matters, including most civil and criminal law. Given the lack of any notion of independent checks and balances in the communist system, the judiciary was politically subordinate to the communist party (as representative of the people). The judiciary was organized in a hierarchy of courts managed by the executive branch (the Ministry of Justice). Prosecutors in the powerful Procuracy oversaw the day-to-day conduct of hearings and other judicial processes. There was no role for constitutional courts, as there was only one source of power—the party.

The legal profession—lawyers, prosecutors, and judges—were trained in socialist law. Like other parts of the profession, the bar association that oversaw lawyers was also controlled by the state, as were the salaries of all professionals. Being a judge was a respectable but not particularly high-status profession, and neither judges nor lawyers were particularly well paid. Since the demise of socialism, there has been rapid growth in the demand for legal expertise to service the new private sector. These professions have seen a consequent change in opportunities, expectations, the level of competition, and resulting salary structures. Many lawyers were quickly able to expand their expertise in new areas of law applicable to market economies, and they thrived. But opportunities and incentives for judges to expand their skills to suit the new economic realities were less available. Thus the perceived quality of judges and their fit with the institutional needs in these emerging market economies deteriorated through the 1990s in many settings.

Citizen mindsets

The mindset of citizens in many countries at the start of transition reflected the long-term impact of a highly centralized state. For example, the 1990 *World Values Survey* included a question on who the respondent believed should manage business and industry: owners, employees, owners and employees together, or the government. As is clear from figure 2.1, citizens in transition countries were much more likely than those in most other countries in the world to say that the government

Figure 2.1 Views of the state and the economy, 1990



Source: World Values Survey.

Note: See appendix 3 for details. Black bars are transition countries or jurisdictions, and E. Germany.

should own and manage business and industry. Attitudes about state institutions and their central role in society were deeply ingrained.

There were, however, significant differences in mindsets and knowledge among citizens of different countries. A key difference between societies of the CIS and those of Central and Eastern Europe (including the Baltics) was that in the latter, socialism had been in place for only about 40 years when transition began in 1990, as compared to 70 in the former Soviet Union. Thus older people still had memories of presocialist forms of property and business organization, and they retained an understanding of concepts of private property and other private rights. It is no coincidence that key milestones in the history of communism came in Hungary and Czechoslovakia, both countries with fairly strong memories of the rights available to individuals in the pre-communist period. The fundamental recognition of rights vis-à-vis the state ultimately played an instrumental role in toppling Soviet-style communism. In Poland, for example, the deep-seated notion of rights helped to create and sustain the Solidarity Movement.

The reform agenda: legislation and institutional change

The transition challenge facing the CEE and CIS countries at the beginning of the 1990s was both enormous and complex. Many of the countries faced tremendous macroeconomic instability, with high inflation, a reduction in traditional sources of fiscal revenue, a drying up of traditional trade links, and illiquid enterprises facing major price shifts and a loss of markets. Many also faced severe political uncertainty, not knowing whether democracy could survive and what type of regime would ultimately prevail. In this chaotic situation any attention to longer-term development concerns—including fundamental judicial reform—had to compete for limited resources and government attention with the overwhelming need to create new political and economic systems. It is perhaps not surprising that domestic reformers and much of the international community initially emphasized political transformation, macroeconomic stabilization, and basic structural reforms (including privatization) over longer-term institution-building needs. Some observers argued from the beginning that transition countries needed to match their emphasis on economic policy reform and the rapid creation of a private sector with efforts at

institutional strengthening, including reform of legal and judicial institutions, to ensure that the new private sector operated in competitive markets and that new legal frameworks were enforced fairly and consistently.⁵ Ultimately, however, the creation or strengthening of legal and judicial institutions took a back seat to passing laws and decrees to support and implement macroeconomic and structural reforms.

In this environment, efforts at legal reform were focused on drafting and quickly adopting new laws and regulations required to build a market economy. Enormous efforts were devoted in all transition countries, for example, to the drafting or amending of constitutions, civil and commercial codes, land and labor laws, and privatization legislation. These laws tended in most countries to be drafted by staff of line ministries, often with donor-financed technical assistance, without extensive consultations among ministries or with outside business groups or lawyers. In some cases this rapid and somewhat closed-door drafting process led to inconsistencies, as noted by a Polish lawyer: “[L]aws are being revised frequently and under time pressure . . . the advisors working on the laws forget their interconnection with other laws, and so there are inconsistencies, and you cannot predict how that can be solved in interpretation . . .”⁶ Throughout this early period fundamental legal institutions remained unchanged. The same court structures and the same judges—with the same legal training, experience, and incentives—remained in place in most transition countries. Judges and judicial systems that had been largely cut off from the development of modern commercial laws, regulations and institutions during the Cold War were ill-equipped to interpret and implement this new economic framework.

Policy makers who promoted these legislative reforms argued that the rapid development of the private sector was needed to consolidate democratic change and would, among other things, create the demand for supporting institutions such as the protection of property rights and effective enforcement of contracts.⁷ Unfortunately, in hindsight it is evident that not all new private sector entities necessarily demanded “good” institutional reforms. Once they were established, some managers of new private firms had an incentive to prefer slow legal and institutional change in order to entrench their monopolistic positions or manipulate corporate governance mechanisms in new firms they controlled to further concentrate ownership.⁸

The relatively slow pace of institutional reform led to a fundamental problem: focused on the specific objective of rapidly producing modern

business-related laws, governments and judicial systems did not always have the institutional capacity to implement and enforce these laws fully or consistently once they were adopted. In the Kyrgyz Republic, one participant in the reform process acknowledged that “[w]e started out drafting laws, saw them passed and now we watch as they are not implemented.” As a result, an implementation gap between the newly adopted commercial laws and their use and enforcement quickly appeared. The lack of effective implementation of laws can have a significant impact on economic development. One study found, for example, that the effectiveness of legal institutions is more important to the provision of external finance in transition countries than the existence of new commercial laws.⁹ Another concluded that the effectiveness of bankruptcy law is a significant determinant of the ratio of private sector credit to GDP as well as the flow of foreign direct investment in transition economies.¹⁰

The relationship between the lawmaking process and institutional reform is in the end very complex. Implementation problems are not unique to transition economies, as well-drafted laws fail to be implemented in practice in many settings around the world. Strengthening of institutions inevitably takes a major commitment of time and resources. On the one hand, adopting laws that cannot be enforced in practice is, at best, an inadequate beginning and, at worst, a counterproductive exercise that can undermine public confidence in the rule of law. On the other hand, legal changes that put new demands for performance on existing institutions can help to spur a process of institutional strengthening over the medium term. In Hungary, for example, a tough new bankruptcy law adopted in 1992 put heavy pressure on the courts and led to significant strengthening of their capacity and the development of an impressive cadre of bankruptcy trustees. In contrast, Poland’s contemporaneous decision to avoid the courts and instead pursue enterprise liquidation and debt workouts through a special out-of-court process may have accomplished the short-term goals of the program, but did little to spur longer-term institutional strengthening in the bankruptcy area.¹¹

Donor support

In a similar vein, donor assistance was often targeted more heavily toward the development of specific commercial laws and regulations than on the reform of implementing and enforcing institutions. Some

donors focused on the production of laws in order to show quick measurable results. Conditionality attached to loans from the international financial institutions frequently reinforced the emphasis on legislation over institution building. However, assistance focused on outputs or provided according to a checklist often did not further the effective implementation of the new commercial legal systems.¹²

It should be noted that even in this early period of transition, some donors did provide support for the beginning stages of institutional reform in the legal and judicial sphere. Their priority was to help create an independent and depoliticized judiciary, free from state control, which could act as a bulwark for the new political and civil rights that the citizens of CEE and the CIS had recently won. In addition to supporting the drafting and adoption of constitutions that enshrined the idea of an independent judiciary, some donor assistance focused on the formal aspects of the judicial system: appointment, tenure, removal, and disciplinary procedures for judges; the development of self-governing bodies for the judiciary; and the creation of judge-controlled training institutes. The transition countries also created new, specialized constitutional courts staffed with new judges (mainly scholars and academics) to hold governments accountable and institutionalize the protection of civil and political rights.¹³ More detailed procedural and organizational changes that could make the courts work “better” by making them more efficient and accessible were usually not included in these early judicial reform efforts.

The World Bank emphasized legislative drafting for commercial, financial, and sectoral reform during the early years of transition, as can be seen clearly in table 2.1, which shows the evolution of the Bank’s legal reform work in Europe and Central Asia. Judicial reform—that is, assistance focused on judges and courts, such as judicial training, case management, alternative dispute resolution (ADR), and procedural

Table 2.1 Evolution of World Bank legal reform projects in Europe and Central Asia
Number of project components

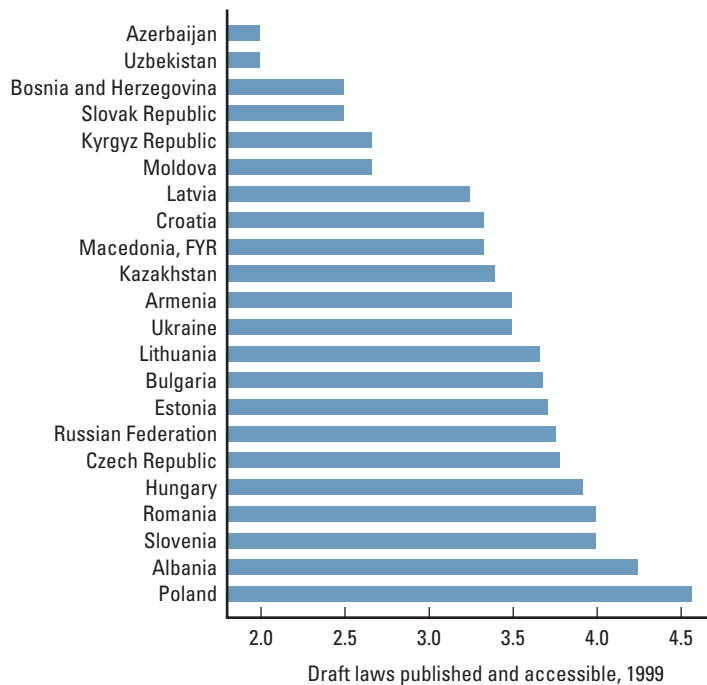
| | Commercial | Financial | Judicial | Sectoral | Privatization | Property Rights |
|-----------|------------|-----------|----------|----------|---------------|-----------------|
| 1990–3 | 12 | 5 | 0 | 6 | 6 | 4 |
| 1994–7 | 25 | 20 | 13 | 6 | 14 | 7 |
| 1998–2001 | 33 | 29 | 27 | 15 | 10 | 7 |

Source: Background data from the World Bank (2002a).

reform—was not taken up until the middle of the 1990s, and only at the end of the first decade of reform were projects with judicial reform components on par with those focused on legislative drafting.¹⁴

Even with all the attention given to drafting laws, the lawmaking process itself received little attention from donors. Some donors provided some early and limited assistance on legislative drafting to transition parliaments (primarily training and assistance in creating a drafting committee of parliamentary staff).¹⁵ Efforts to broaden participation in the lawmaking process to include inputs from enterprises, their lawyers, and the judges who would use and be affected by the law were minimal.¹⁶ A Russian lawyer advised “We should use practitioners and judges, not just academics, to comment on draft legislation.” As figures 2.2 and 2.3 illustrate, by the end of the decade enterprise managers and lawyers in

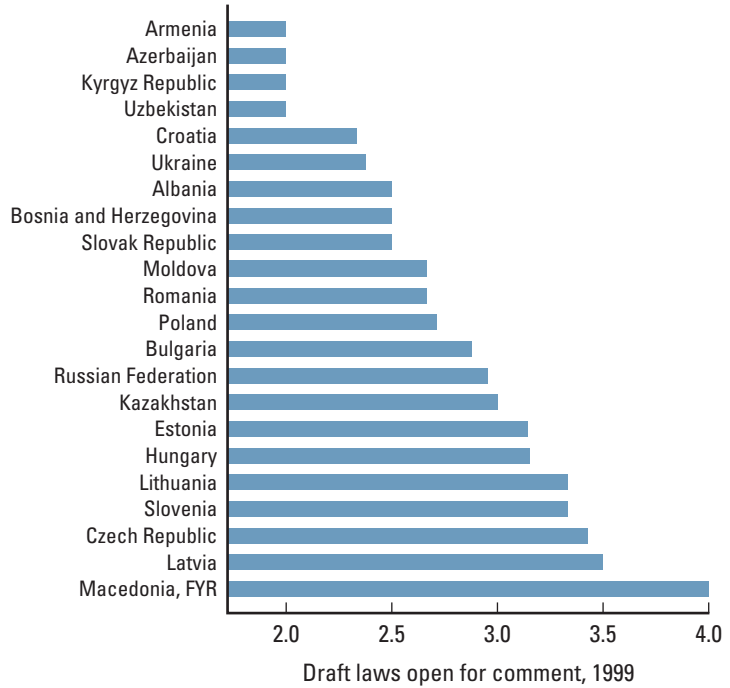
Figure 2.2 Accessibility of draft laws, 1999



Source: EBRD Legal Indicator Survey 1999.

Note: See appendix 3 for details. 1=never, 2=rarely, 3=sometimes, 4=frequently, 5=almost always.

Figure 2.3 Ability to comment on draft laws, 1999



Source: EBRD Legal Indicator Survey 1999.

Note: See appendix 3 for details. 1=never, 2=rarely, 3=sometimes, 4=frequently, 5=almost always.

many countries in the region felt that they had little access to or influence over the legislative drafting process.

The EU imperative

The European Union and its accession process have exerted a tremendous influence on the direction, pace, and progress of legal and judicial reform in the transition countries. Starting in 1991 and 1992 with the signing of the first Association or Europe Agreements, through the submission of the first Union membership applications in the middle of the decade, to the opening of the first formal accession negotiations and accession partnership agreements in 1998, the hope of joining the prosperous countries of the Union has motivated the transition countries to undertake politically

difficult and complex reforms. By promoting and requiring the approximation of local laws to its *acquis communautaire* (that is, the laws, rules, and regulations governing the EU), the EU has served as a standard setter. It has also been an important donor, providing technical assistance, material, and grants to support the adoption of the *acquis* (and later its implementation). Lastly, the EU has acted as an assessor or auditor, “grading” the accession progress of candidate countries in its annual reports and setting targets for further reforms.

The influence of this EU imperative has varied geographically. The countries of Central and Eastern Europe and the Baltic states have felt the EU’s influence most strongly. As one moves further east through the region, this influence has been less pronounced, particularly in the countries of Central Asia and the Southern Caucasus, which have had little or no expectation of entering the Union. There appeared little hope that the western Balkan countries would be allowed to join the accession process during the period of civil conflict in the early and middle 1990s. The situation changed dramatically after the conflict ended, when the EU initiated a new Stabilization and Association Process with these countries that envisioned the rapid adoption of the *acquis* and offered them a firm EU integration perspective. While certainly not the only driver or determinant of the pace and direction of legal and judicial reform in the region, the “accession attraction” has had a marked impact on the impetus for legal reform.

The EU accession process, with its focus on adopting the *acquis communautaire*, has tended to reinforce the priority given by transition countries to lawmaking (often at a rapid pace—see box 2.1) over longer-term institution building. At the same time, this external attention and the

Box 2.1 The drive to pass laws to meet European Union deadlines

The drive for the wholesale adoption of laws on a strict EU accession timetable is pricelessly illustrated by a news article in early 2004 from Latvia. Less than a month before becoming a full member of the European Union, the Baltic News Service stated:

Latvian Government Still To Pass 14 Laws, 137 Regulations Before EU Accession In May.
Dateline: Riga, Apr 13.

Although most of the laws and regulations passed by the Latvian government and parliament in the past month have been related to the Baltic state’s EU accession on May 1, the government is yet to pass 137 EU-related regulations and 14 laws in under three weeks time.

Source: Baltic News Service, April 13, 2004.

popular desire to join the EU galvanized support for necessary legislative reforms across party lines in the accession countries. The EU has also emphasized the efficiency, effectiveness, and accountability of judicial institutions. In its annual Regular or Monitoring Reports on the accession countries, the European Commission has pointed to weaknesses in the implementation of laws, particularly the lack of capacity and other problems in the judiciary, as key constraints on the accession process. In the December 1997 Luxembourg Declaration launching the enlargement process and the accession partnerships, the Council identified “the reinforcement of administrative and judicial capacity” as one of the priority aims of its future technical assistance to the accession countries.¹⁷ This recognition led the Commission to allocate approximately 30 percent of the EU’s preaccession assistance for judicial and administrative strengthening, while the remaining 70 percent continues to fund legislative reform to meet the needs of the *acquis communautaire*.

While the *acquis* does not address or provide standards for judicial operations, the Commission’s focus on candidate countries’ capacity to implement and apply the rules and regulations in the *acquis* has raised the importance of institutional reform in the judicial system. European Commission attention and advice have emphasized the objectives of fair trials and an independent judiciary contained in United Nations (UN) documents, the European Convention on Human Rights, and various Council of Europe (COE) recommendations.¹⁸ The COE has focused on putting these standards into practice by providing assistance to improve the efficiency and fairness of judicial procedures.¹⁹ The formal enforcement body for the European Convention is the European Court of Human Rights (ECHR). In 2003, over half of the ECHR’s caseload concerned Council of Europe member states’ alleged violations of the European Convention’s right to a “fair trial” (Article 6). Transition countries, most notably Poland, Romania, and the Slovak Republic, were often subjects in these cases.²⁰

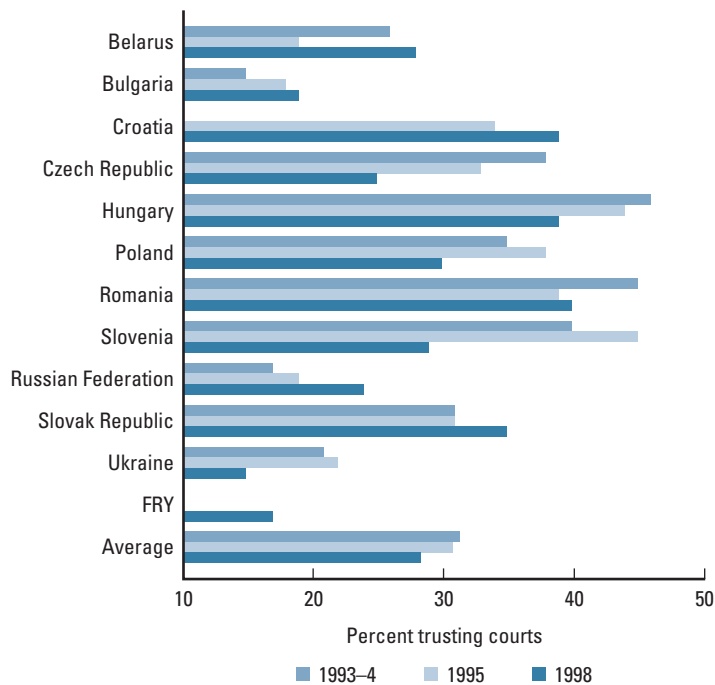
Citizens’ views on the first reform decade

The perceptions of the courts inherited from the old regime evolved throughout the region during the 1990s. A useful data source for analyzing how citizens viewed the courts in this decade is the series of surveys conducted by the Centre for the Study of Public Policy at the University

of Strathclyde. These large-scale public opinion surveys are unique in that nearly identical questions were asked in many countries through multiple rounds. One question of particular interest concerns the level of trust that the respondent places in various bodies and institutions, among them the courts. Figure 2.4 shows the percentage of the population that said they trusted the courts during the course of the decade, while figure 2.5 shows the level of trust relative to two other broad institutions of the state, the government and parliament.

Throughout the decade, less than half of the respondents in any given transition country said they trusted the courts. By the end of the decade, no more than 40 percent of respondents in any transition country said they trusted the courts. Levels of trust tended to be higher in CEE than in

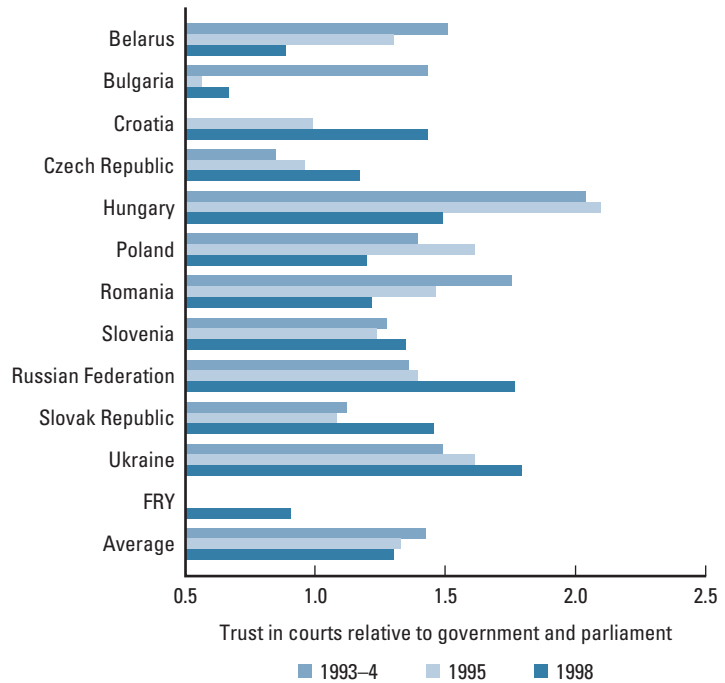
Figure 2.4 Trust in courts, 1993–8



Source: Centre for the Study of Public Policy.

Note: See appendix 3 for details. FRY = Federal Republic of Yugoslavia (now Serbia and Montenegro); FRY not included for 1993–4 and 1995, Croatia not included for 1993–4. Average based on countries with full data.

Figure 2.5 Trust in courts relative to parliament and government, 1993–8



Source: Centre for the Study of Public Policy.

Note: See appendix 3 for details. FRY = Federal Republic of Yugoslavia (now Serbia and Montenegro); Not surveyed: FRY (1993–4 and 1995), Croatia (1993–4), Russia (Government). Average based on countries with full data.

CIS countries. Several CEE countries that had relatively high levels of trust early in the decade experienced declines by 1998, most notably the Czech Republic, Poland, and Slovenia, and to a lesser extent Hungary and Romania. With the exception of the Czech Republic and Slovenia, these declines in trust in the courts came in both absolute terms and relative to trust in other institutions. It is possible that as legislation became more sophisticated and complex, institutions charged with applying and enforcing these laws—the courts—did not keep pace.

In Bulgaria, trust in the courts was low in absolute terms throughout the period and fell drastically relative to other institutions. Citizens in both Bulgaria and the Federal Republic of Yugoslavia (now Serbia and Montenegro) clearly ranked courts very poorly by the end of the decade.

At the other extreme, Ukraine stands out for having declining trust in the courts from an already low base, although figure 2.5 makes clear that courts were still rated more favorably than the government or parliament. Only two countries showed unambiguous improvement during the 1990s in levels of trust in the courts, both in absolute and relative terms: the Russian Federation²¹ from a relatively low baseline and the Slovak Republic from a relatively high one.

Although the trends exhibited in figures 2.4 and 2.5 are generally more negative than positive, it should be noted that by 1998 courts were still more trusted than the other broad institutions of state, the government and the parliament. In only three of the twelve countries covered by the survey [Belarus, Bulgaria, and FRY (Federal Republic of Yugoslavia—now Serbia and Montenegro)] was this not the case. While the relative paucity of attention to judicial reforms during the decade of the 1990s may have eroded already low confidence in the courts to some degree, other institutions of state were equally beset by lack of trust. As a result of myriad reforms, the first decade of transition closed with a reduced role for the state in the incipient market economy, juxtaposed with a view that state institutions were too weak to be effective.

Notes

1. Public law governs the relationship between individuals (citizens, companies) and the state and addresses the structure and operation of the government itself. Constitutional law, administrative law, and criminal law are thus generally subdivisions of public law.
2. Administrative law deals with the decision making of administrative tribunals or boards and authorities that are part of a state regulatory scheme.
3. Private law is the area of law that governs the relationships between individuals or groups without the intervention of the state or government. It includes, among other laws, the law of contract, torts, and the law of obligations.
4. Gray, Ianachkov, Hanson, Heller, Ostas, and Stiblar 1993.
5. See, for example, Murell 1992.
6. Dietrich 2000.
7. This prioritization was clearly seen, for example, in the economic reform and privatization efforts undertaken in the Czech Republic and Russia.

8. Black, Kraakman, and Tarassova 2000.
9. Pistor, Raiser, and Gelfer 2000.
10. EBRD spring 2000.
11. Gray and Baer 1996.
12. Carothers 1996, 1999.
13. In general, these courts are credited with performing better than expected. See Schwartz 1999.
14. See appendix 2 for a summary of recent World Bank activities in support of judicial reform in transition countries.
15. deLisle summer 1999.
16. A program director in the Kyrgyz Republic noted, "There is no legislative process at all. We need to introduce the idea of a public comment period." Dietrich 2000.
17. Luxembourg European Council, Presidency Conclusions, Doc/97/24 (December 13, 1997).
18. The 22 International Covenant on Civil and Political Rights (adopted and opened for signature, ratification, and accession by General Assembly resolution 2200A (XXI) of December 16, 1966); U.N. Basic Principles on the Independence of the Judiciary, (endorsed by the General Assembly resolution 40/32 of 29 Nov 1985); European Convention for the Protection of Human Rights and Fundamental Freedoms, (Rome, November 4, 1950); COE Recommendation No. R(84)5 on the Principles of Civil Procedure Designed to Improve the Functioning of Justice (adopted by the Committee of Ministers on February 28, 1984); and COE Recommendation No. R(94)12 on the Independence, Efficiency and Role of Judges (adopted by the Committee of Ministers on September 11, 1995).
19. See <http://www.coe.int/cepej>.
20. The caseload of the European Court of Human Rights is available at: <http://www.echr.coe.int/Eng/Judgments.htm>.
21. The questionnaire for Russia did not include "government," so the numbers in figure 2.5 represent trust in courts relative to parliament only.

3

Legal and Judicial Institutions Ten Years into Transition

BY THE BEGINNING OF THE 21ST CENTURY, MOST TRANSITION countries had experienced nearly a decade of political, social, and economic reforms, often in fits and starts, in various mixes, and with varying degrees of intensity. The same is true for legal and judicial reforms. As outlined in the previous chapter, the experience of many countries emphasized passing laws over institutional reform and judicial independence over accountability and efficiency. Near the end of the decade, reformers and donors began to develop tools to analyze and evaluate the shape of the region's legal and judicial systems and the effect these systems had on economic development, whether at the level of the overall economy or at the level of an individual enterprise. This chapter draws on these data to explore the state of the judiciary 10 years into the transition process.

The “implementation gap”

As described in the previous section, the first decade of reform emphasized passing legislation to support a market economy, with relatively less attention to the institutional reform needed for effective implementation. Figure 3.1 shows indicators of the extent of commercial legislation existing in 1999 (“legal extensiveness”) and the degree to which it was being implemented at that time (“legal effectiveness”).

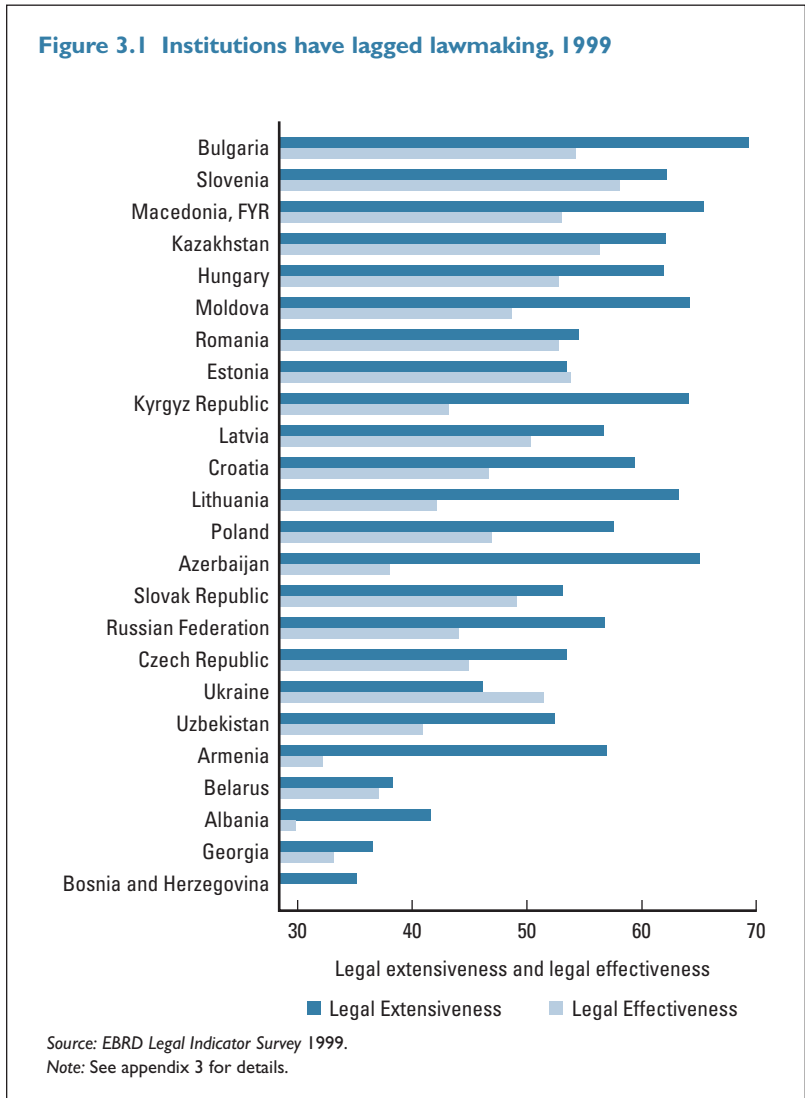
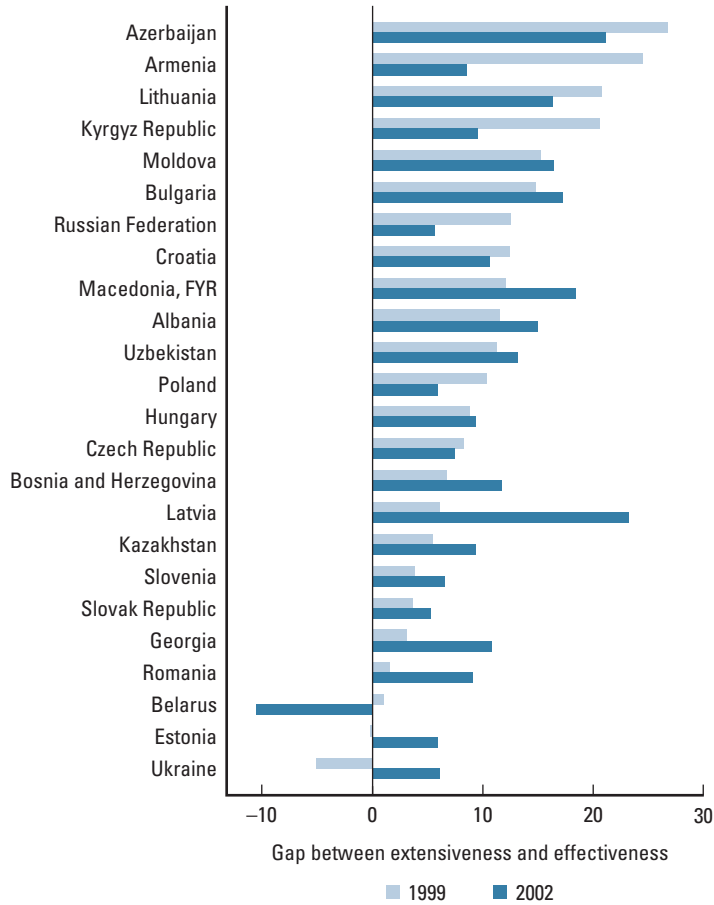


Figure 3.2 shows that this “implementation gap” that appeared early in the transition process persisted and in many cases (including countries in southeastern Europe, as well as Estonia, Georgia, Latvia, and Ukraine) expanded into 2002. The only country in which implementation did not lag lawmaking in 2002 was Belarus, where policy reforms have been slow.

Figure 3.2 Changes in the “implementation gap,” 1999 and 2002



Sources: EBRD Legal Indicator Survey 1999 and 2002.
 Note: See appendix 3 for details.

Court performance

We turn now to assessments of the courts along the dimensions of independence, efficiency, affordability, transparency, and accountability, and the ability to enforce decisions. The ABA–CEELI JRI provides a useful tool for beginning to examine these issues. Figure 3.3 shows the

Figure 3.3 Assessments of aspects of the judiciary in 14 transition economies



Source: ABA-CEELI Judicial Reform Index.
 Note: See appendix 3 for details.

average rating across all 14 countries covered by the JRI on each of the JRI’s 30 different indicators.¹ The JRI rates each dimension as positive, neutral, or negative. For the purposes of this analysis, these have been assigned values of +100, 0, or -100. An average score of 0, therefore, means that the number of countries with ratings of positive exactly equals the number of countries with ratings of negative.

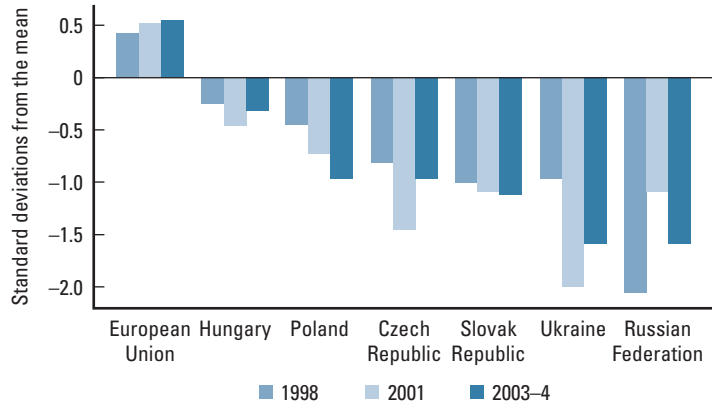
Independence

The judicial reforms that were the primary focus during the 1990s emphasized the structural issues needed to reinforce the judiciary's role as an equal and independent branch of government, as laid out in the new or revised constitutions adopted throughout the region. As is clear from figure 3.3, relatively more progress has been made on independence issues than on more detailed areas such as court management. Highest marks go to reforms in support of judicial immunity and guaranteed tenure, while the lowest marks are reserved for such management and transparency issues as maintaining trial records and publishing court decisions. Aspects of management of the judiciary that have been the focus of reforms elsewhere in the world, such as systems of case and court management and human resources, were not initially the center of attention in transition countries.

A hallmark of independent and impartial legal systems is the ability of people and firms to use courts to challenge government actions and decisions. During socialist times the judicial system was geared toward defending the rights of the state. At the beginning of transition, the idea of a court overturning a government decision was simply outside the realm of possibility for many people. By the late 1990s, after a decade of reforms, the idea may have seemed less extraordinary, but in many countries there was still little confidence on the part of the public in the ability of citizens or courts to challenge the government through the legal process. For a small number of countries, an indication of how firms view this issue is provided by the *Executive Opinion Survey* (EOS) conducted annually by the World Economic Forum, in which firms were asked about the legal framework for challenging government decisions. The questions changed somewhat from year to year, so it is difficult to identify absolute trends from these data alone. It is possible, however, to examine how countries or subsets of countries rank compared to each other in any particular year.

Figure 3.4 provides an indication of how firm responses in each country compared with those in other transition countries and the 14 EU countries included in the survey. Russia showed steady improvement in perceived independence, compared with other countries in the survey, from 1998 to 2001, and declined for the next two years. Ukraine showed the nearly opposite pattern, declining steadily through 2001, and then recovering slightly. Poland exhibited a slow but steady erosion of citizens'

**Figure 3.4 Are courts independent enough to challenge the state?
Relative perceptions of firms, 1998, 2001, and 2004**



Sources: World Economic Forum, Global Competitiveness Reports 1998, 2001, and 2003–4.
Note: See appendix 3 for details. EU includes only subset of countries with available EOS data.

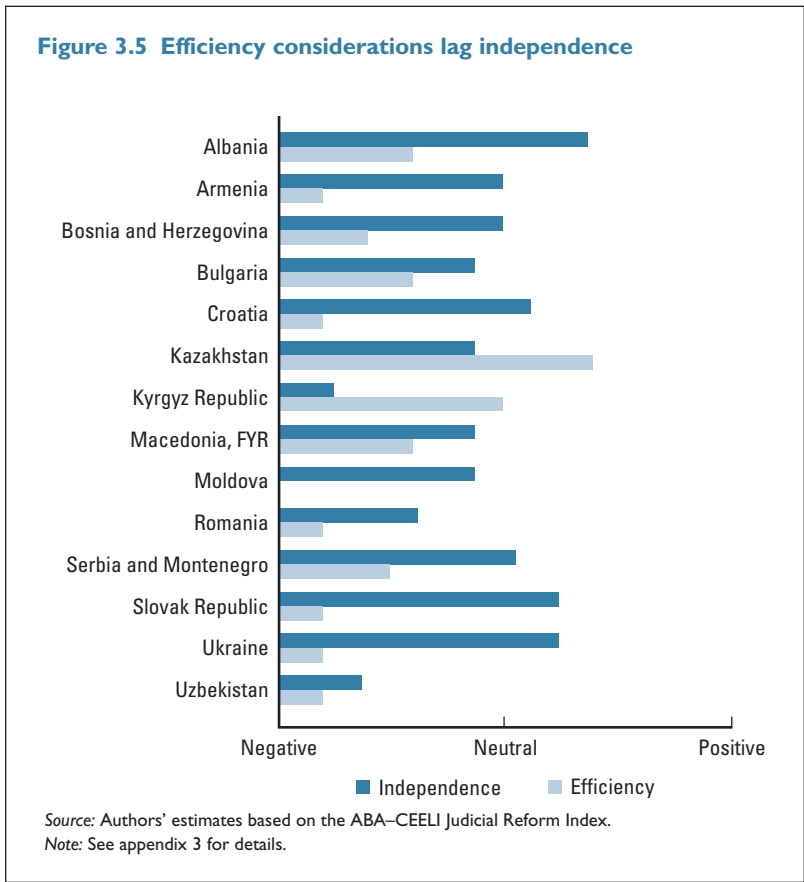
perceptions of the courts’ ability to challenge government actions compared to other countries, while the Czech Republic has shown a recent improvement, following a dramatic decline around 2000. Because the chart shows assessments relative to other countries, the slightly positive trend for the EU group of countries means only that the average assessments of the impartiality of the legal system for challenging government actions in those 14 countries were improving *relative* to the 6 non-EU² countries shown in the chart. In other words, there is as yet no evidence of convergence or “catching up” of transition countries to EU practice along this dimension of court performance.

Given the early emphasis on establishing independent judiciaries in the transition countries, this result is a bit disappointing. Focusing on the formal structures and instruments that help to make a judiciary independent has apparently not yet been perceived as successful, at least by the firms surveyed by the World Economic Forum. Some judiciaries in transition countries still remain subject to political influence in the selection and disciplining of judges. Most have little influence over the allocation of budget to the judiciary and little control over how these funds are spent. Two types of actions are needed: (1) actions to depoliticize the recruitment, appointment, and career progress or termination of judges (which

is often within the purview of judicial councils); and (2) actions to give judiciaries more influence over the use of court resources and autonomy over their administration. [For example, the former Yugoslav Republic (FYR) of Macedonia’s judges received power over their budget in early 2004.] Establishing a judicial system that is free from politicization, is capable of managing and administering its own human and capital resources, and is able to minimize corruption in its ranks through self-regulation and effective prosecution will take more time, effort, and resources.

Efficiency and affordability

The positive albeit limited progress that has been made on judicial independence stands in sharp contrast to performance with regard to efficiency. Figure 3.5 shows the average ABA–CEELI measures



related to both efficiency and independence for each of 14 transition countries.³ In all but two of these countries—Kazakhstan and the Kyrgyz Republic—the average assessments related to independence exceed those related to efficiency. Kazakhstan is the only country covered by the JRI with an average positive rating for efficiency, perhaps explained by the additional human and financial resources that the Kazakh Government has put into its judicial system.⁴

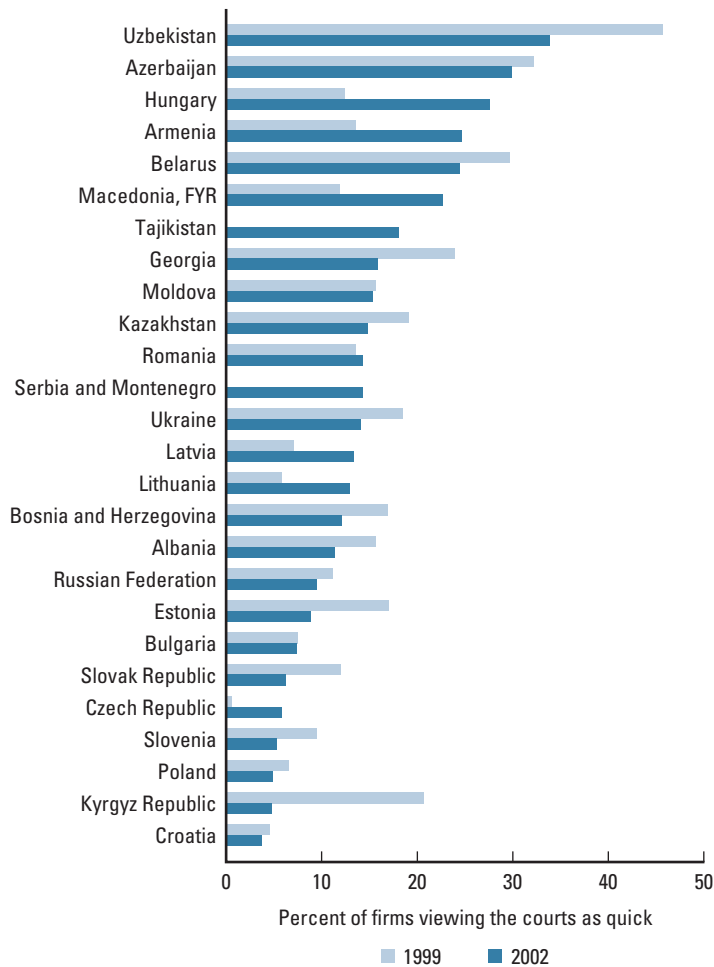
The scant attention paid to the efficiency of the judiciary, at least during the first decade of transition, is evident most concretely in the lack of attention paid to the issue of court records and statistics (figure 3.3). Statistics were kept and compiled in many countries, but they were often based on poorly defined or inappropriate methodologies and almost never analyzed or employed as a management tool. The old adage “what gets measured gets managed” was clearly understood in the arena of macroeconomics; for example, among the very first capacity-building exercises that the IMF undertook in transition countries in the early 1990s were the establishment of a system for generating a meaningful consumer price index and the training of staff to collect the data and calculate the index. When it comes to judicial reform, however, reformers in many countries continue to make decisions based on faulty statistics, or none at all. Fifteen years after the fall of the Berlin Wall, efforts to improve the system of court statistics are just beginning (or have yet to begin) in many countries. In Albania, Armenia, Croatia, and FYR Macedonia, for example, case management and court administration systems are now being put in place to help fill this statistical and knowledge gap.

The issue of record keeping stretches beyond statistics. Practices that are taken for granted in many countries, such as the maintenance and public availability of trial records, remain undeveloped in many transition countries. Indeed, of the 30 indices in the JRI, the only one that is rated negative in every single country where the JRI has been performed is that of the maintenance of trial records (figure 3.3).⁵

From the perspective of firms, the ability to adjudicate disputes in an efficient and timely manner helps reduce uncertainty in actual or potential business deals. In the BEEPS surveys, respondents were asked whether they agreed with various statements about the courts, including important aspects such as fairness, honesty, ability to enforce decisions, affordability, and speed. The statement that received the lowest marks for the transition countries as a whole was that “courts are quick,” to which only 15 percent of firms in CEE and the CIS agreed in 1999, and even

fewer in 2002. There were variations in trends over time among countries, however. Figure 3.6 shows the percentage of firms saying courts were quick in both 1999 and 2002. Georgia, the Kyrgyz Republic, and Uzbekistan received significantly lower ratings in 2002, as did Estonia

Figure 3.6 Assessments of courts as “quick,” 1999 and 2002



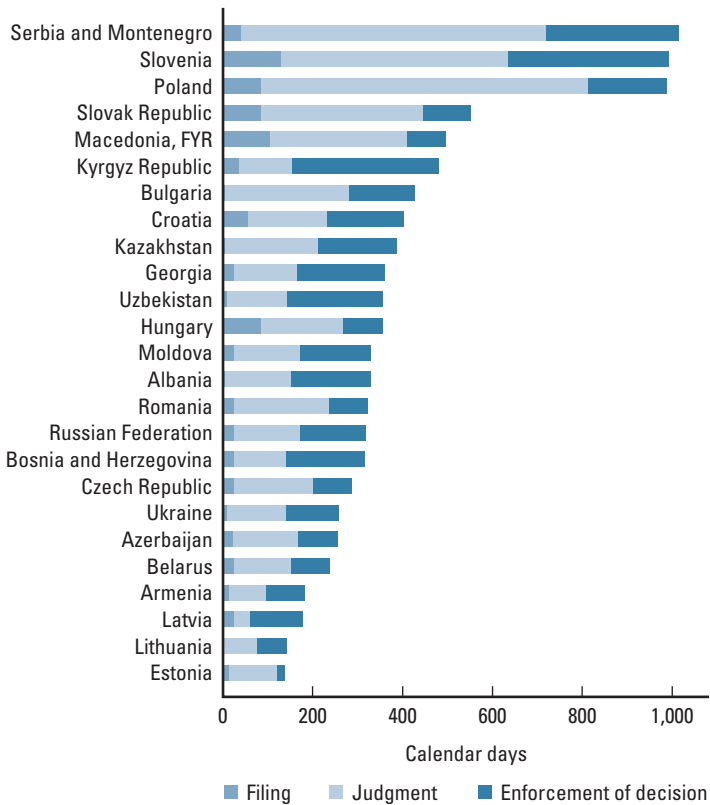
Sources: BEEPS1; BEEPS2.

Note: See appendix 3 for details. SAM and Tajikistan were not surveyed in 1999. Changes statistically significant for Armenia, Czech Republic, Estonia, Georgia, Hungary, Kyrgyz Republic, Latvia, Lithuania, Macedonia, FYR, Slovak Republic, and Uzbekistan.

and Slovak Republic. In contrast, Armenia, the Czech Republic, Hungary, Latvia, Lithuania, and FYR Macedonia showed significant improvement in the perceived speediness of courts between 1999 and 2002. (Changes from 1999 to 2002 in other countries were very small and not statistically significant.) But in all countries major improvements are still needed.

A second source of data provides a complementary perspective on the efficiency of the court system. The *Doing Business Survey* polls practicing law firms in countries around the world to find out about the efficiency of court proceedings and constraints on firms. Respondents are asked to consider a hypothetical example of collecting on a debt and to estimate how long it takes to handle each of the many steps involved. Aggregating these steps into three broad time periods—pretrial, trial, and enforcement—provides a view of where bottlenecks occur. Figure 3.7 presents responses from transition countries. While there is considerable variation, it is worth noting that in most transition countries, it takes more than 200 days to collect on an unsecured debt through the courts, and in three countries—Poland, Serbia and Montenegro, and Slovenia—it takes nearly three years. Even bars that look small in figure 3.7 still suggest a significant time delay for the simple task of collecting on a debt.⁶ As illustrated in figure 3.8, the average length of time required to collect on a debt in transition economies is nearly double the average time required in higher-income Organisation for Economic Co-operation and Development (OECD) countries, although it is similar to the time required in Latin America, the Middle East, and Sub-Saharan Africa (where legal and judicial reform is also an enormous challenge). One approach to reducing backlog and improving efficiency is to upgrade the IT infrastructure of courts. While this approach can be very effective, care should be taken to introduce the technology properly, as explained in box 3.1.

Another indicator of court performance is affordability. For the transition countries as a whole, assessments of the affordability of courts deteriorated significantly between 1999 and 2002, and the same is true in many individual countries, including the Czech Republic, Georgia, Hungary, Kazakhstan, FYR Macedonia, Romania, Russia, the Slovak Republic, and Uzbekistan (figure 3.9). The only notable exception is Poland, which improved tremendously from a low assessment by firms in 1999. In Georgia, one of the countries with deteriorating perceptions of affordability, a plaintiff could spend almost 12 percent of a claim on filing, appellate, and enforcement fees, and one judge has noted that nearly 75 percent of litigants cannot afford these fees.⁷

Figure 3.7 The time delay to collect on a debt through courts

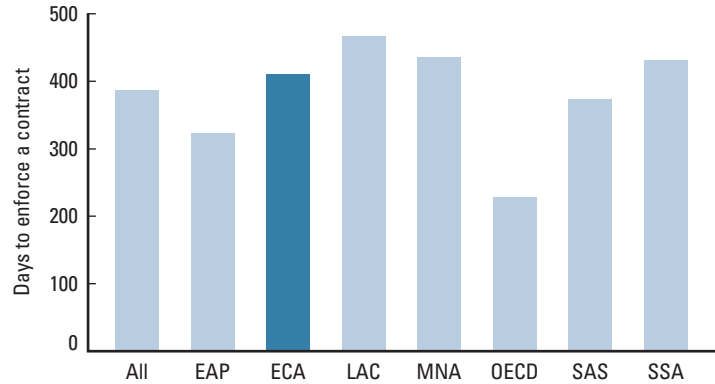
Source: Doing Business database, World Bank 2004.

Note: See appendix 3 for details.

Box 3.1 The need to upgrade technology

The provision of computer hardware and software to courts is often seen as a panacea for inefficient and backlogged judicial systems. Lessons from ongoing judicial reform projects in Albania, Armenia, Croatia, and FYR Macedonia reveal that computers, software, and other IT assistance have the greatest impact on the efficiency of court operations when they are (1) developed and designed with leadership and detailed input from the judges who will benefit from them; (2) closely integrated with existing procedural rules and case flow practice; and (3) accompanied by a clear commitment from the judiciary to provide the necessary financial and human resources to maintain the IT systems. Computer systems, particularly case management software, can also strengthen judicial accountability by building in transparency through public access to information (often through Internet links to judicial information and decisions) and by facilitating the random assignment of cases.

Figure 3.8 Average length of time to collect a debt in various regions



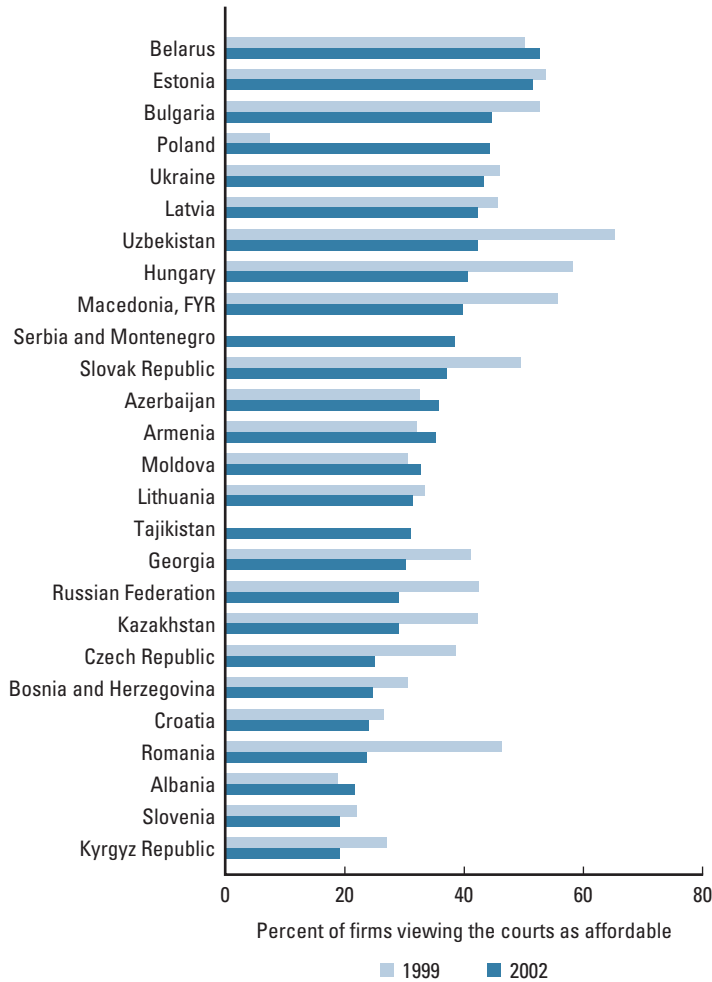
Source: Doing Business database, World Bank 2004.

Note: See appendix 3 for details. EAP = East Asia and the Pacific; ECA = Europe and Central Asia; LAC = Latin America and the Caribbean; MNA = Middle East and North Africa; OECD = Organisation for Economic Co-operation and Development; SAS = South Asia; SSA = Sub-Saharan Africa.

Transparency and accountability

Surveys of firms and of the general public about corruption often identify the courts as among the bodies perceived to be the most corrupt. In some sense this is not at all surprising, given the wide discretion and monopoly in decision making that judges have. But what about accountability? In an effort to create a truly independent judiciary, many transition countries did not place a similar early emphasis on the institutions and rules, such as a system of judicial inspection and discipline, needed to ensure that independent judges remain accountable for their decisions and actions. Although the need to emphasize judicial independence was understandable after decades of communist rule, independence needs to be coupled with accountability. In figure 3.10, aspects of the judiciary from figure 3.3 are aggregated into rudimentary indicators of independence on the one hand and accountability and transparency on the other. While there is some positive correlation among these indicators, it is relatively slight. More important, however, is the fact that for nearly every country—Romania being the exception—the index of independence is higher than the index of accountability and transparency.

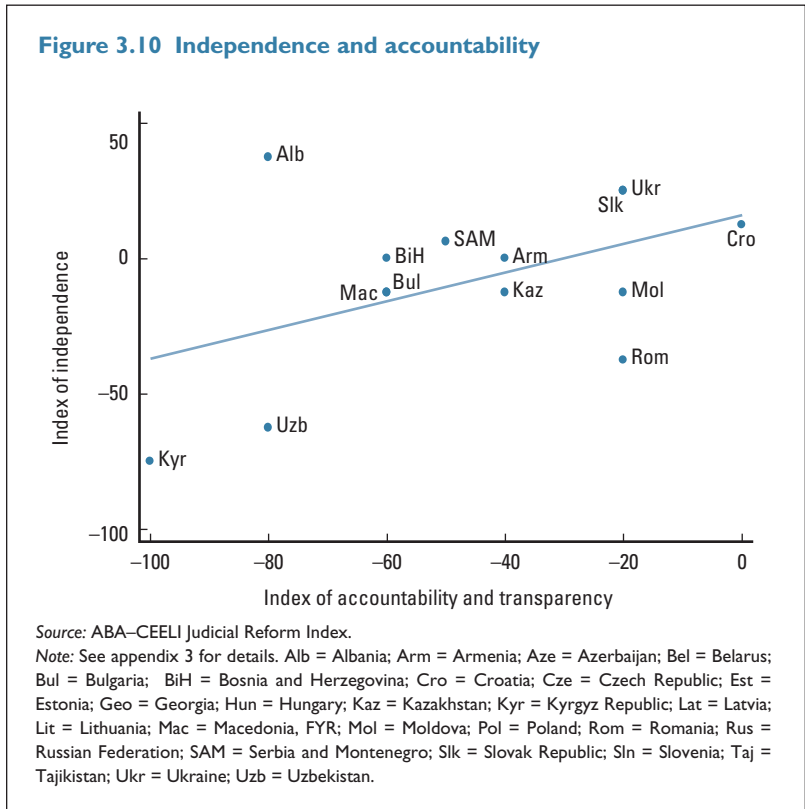
Figure 3.9 Assessments of courts as “affordable,” 1999 and 2002



Sources: BEEPS1; BEEPS2.

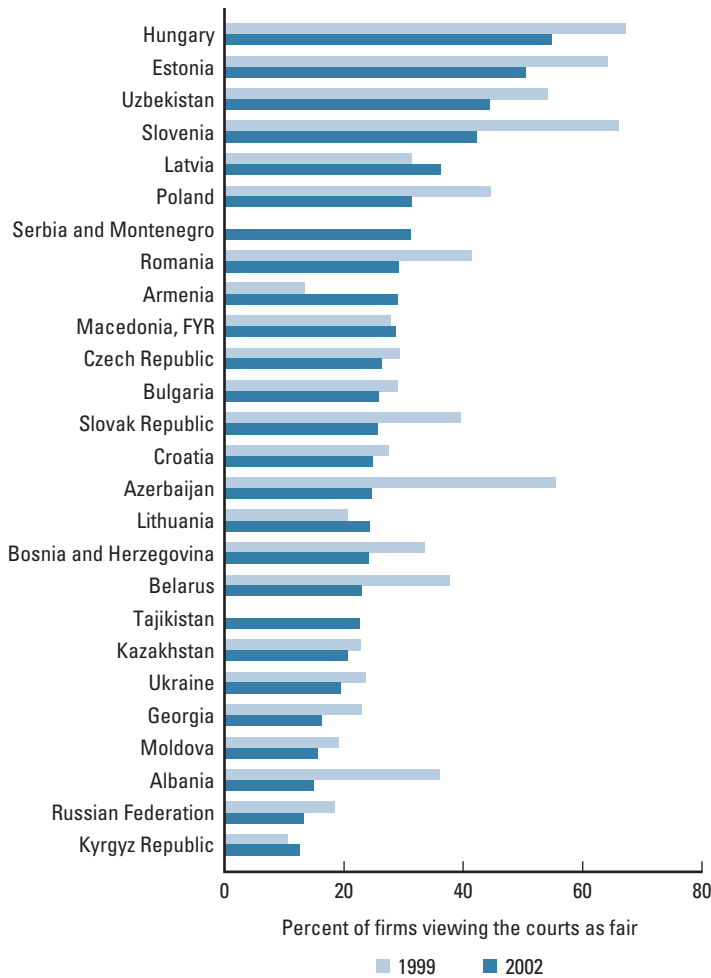
Note: See appendix 3 for details. SAM and Tajikistan were not surveyed in 1999. Changes statistically significant for Czech Republic, Georgia, Hungary, Kazakhstan, Macedonia, FYR, Poland, Romania, Russian Federation, Slovak Republic, and Uzbekistan.

Figure 3.11 shows how firms in transition economies rate their courts in terms of fairness, and figure 3.12 shows assessments of honesty. Although firms were somewhat more likely to say that courts are fair than they are to say they are quick, the assessments are poor—with fewer



than half (and generally fewer than a third) of respondents viewing courts as fair—in almost every country. Moreover, the differences between 1999 and 2002 are striking for many countries and for the region as a whole. No other aspect of court performance experienced as large a decline in favorable assessments as court fairness. Significant declines occurred in more advanced EU Accession countries (such as Estonia, Hungary, Poland, Slovak Republic, and Slovenia) as well as in transition economies in southeastern Europe and the CIS (such as Albania, Azerbaijan, Belarus, Bosnia and Herzegovina, Romania, Russia, and Uzbekistan). Armenia was the only country where significantly more respondents viewed the courts as fair in 2002 than in 1999. Assessments of the honesty of courts also declined in many countries, most strikingly in Albania and in Azerbaijan, and to a lesser extent in Hungary, the Kyrgyz Republic Poland, and Slovenia. Again, Armenia stood alone in showing significant improvement, albeit from a very low base.⁸

Figure 3.11 Assessments of courts as “fair,” 1999 and 2002



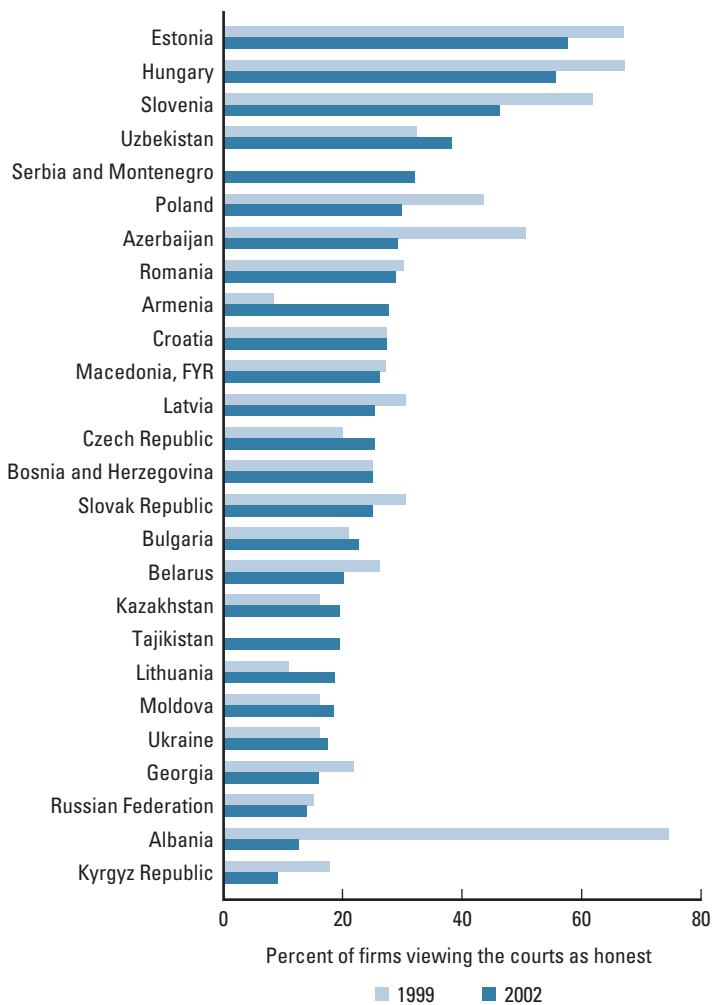
Sources: BEEPS1; BEEPS2.

Note: See appendix 3 for details. SAM and Tajikistan were not surveyed in 1999. Changes statistically significant for Albania, Armenia, Azerbaijan, Belarus, Bosnia and Herzegovina, Estonia, Hungary, Poland, Romania, the Russian Federation, Slovak Republic, Slovenia, and Uzbekistan.

The perception of honesty or dishonesty, of course, is in part a proxy for the perception of corruption.⁹ The BEEPS also asked firms how frequently they must make unofficial payments when dealing with the courts. Interestingly, while the perception of corruption in the courts may have increased

between 1999 and 2002, actual reported experiences with corruption in the region as a whole appear to have decreased (figure 3.13).¹⁰ The greatest improvements occurred in Azerbaijan, Lithuania, and Moldova. The responses for Azerbaijan are perhaps the most surprising, since firms in that country gave significantly more negative assessments of the fairness

Figure 3.12 Assessments of courts as “honest,” 1999 and 2002



Sources: BEEPS1; BEEPS2.

Note: See appendix 3 for details. SAM and Tajikistan were not surveyed in 1999. Changes statistically significant for Albania, Armenia, Azerbaijan, Hungary, Kyrgyz Republic, Poland, and Slovenia.

and honesty of courts in 2002 than in 1999, while at the same time reporting a large decline in the prevalence of unofficial payments. Similarly, Albanian respondents reported a large decline in their perception of the honesty of courts, while also reporting a significant decrease in unofficial payments, albeit from a very high level (the highest in the region in 1999). These anomalies may reflect a lag in how perceptions change compared to actual practice, or they may reflect the complexity of institutional behavior and the fact that dishonesty is not always connected with bribes.

From a policy perspective, a large number of reforms could be implemented to help reduce corruption in courts, including reforms in the way judges are hired and promoted, in how cases are assigned, and in the rules on discipline and tenure. More broadly, the operation of courts and judges could be made more transparent by publishing decisions and by strengthening the nongovernmental organizations (NGOs), media, and other civil society organizations (CSOs) that monitor the judiciary. Many of the judicial reforms that have been undertaken have centered on human resource issues. Several countries (for example, Georgia and FYR Macedonia) have increased judicial salaries, while others have implemented systems of testing for judges (for instance, Albania), sometimes with an entire cohort effectively fired and required to reapply for their own jobs (for example, Georgia). Increasing salaries relies on the assumption that low salaries are causing otherwise honest court personnel, especially judges, to either become involved in corruption or to take their skills elsewhere. Firing judges and requiring them to reapply essentially assumes that there is a pool of available labor elsewhere with the requisite skills and willingness to replace them.

Yet it is an open question whether there is merit to either of these assumptions, and some understanding of the labor market for legal skills would help support informed policy making. It is no doubt true that early in the transition process, the private sector's expanding demand for legal expertise, combined with a fairly tight supply of such expertise, led in many countries to a rapidly growing disparity between salaries in the private sector and salaries of public sector legal professionals (including judges, clerks, prosecutors, and university professors). Restrictions on entry and apprenticing, licensing, and other practices have all effectively limited the supply of legal skills and have driven up the wages of lawyers in the private sector even further. As in many countries around the world, the legal profession in CEE and the CIS is essentially self-regulating, with the professional bar handling licensing, testing, and educational

standards. Yet in the transition setting this self-regulation is new and not too effective, and the cartel-like aspects of the legal profession—present in every country to some extent—tend to have particularly strong effects. (This may be changing in some countries. In Poland for example, the Constitutional Court recently decided that it was unconstitutional to limit entrance into the profession.) Wages in the public sector, however, are not market determined, and the official salaries of judges amount to a fraction of salaries in the private sector.

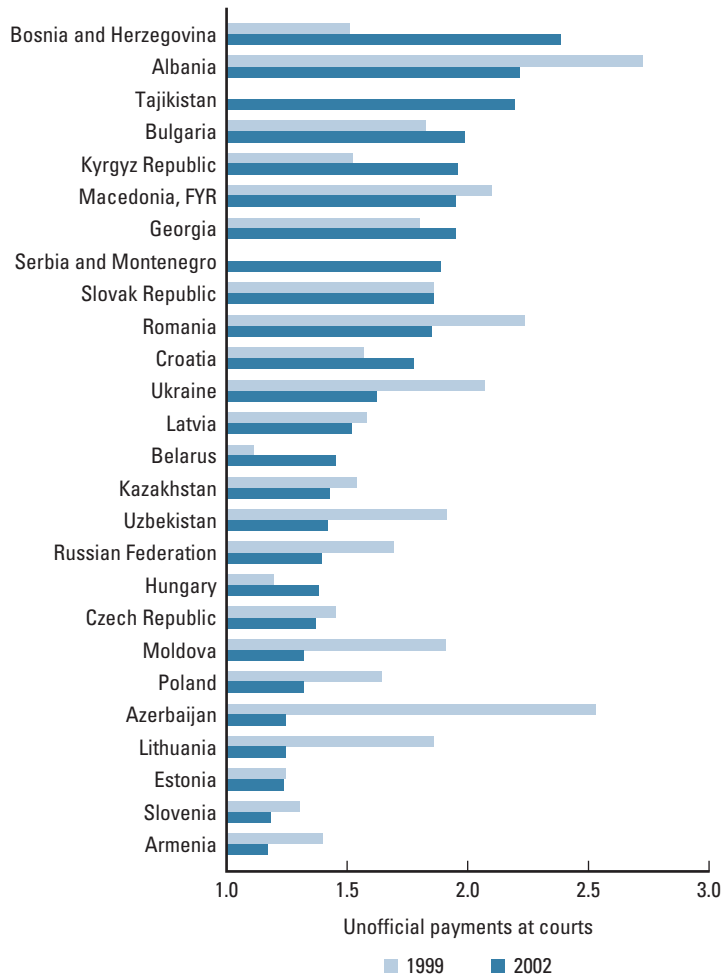
Raising judicial salaries will not necessarily solve accountability problems. Bosnia and Herzegovina tripled the wages of judges, but problems persist: The highest prevalence of unofficial payments at court in 2002, according to firms in the BEEPS, was in Bosnia and Herzegovina (figure 3.13). Indeed, *relative* salaries within the legal profession are correlated with perceptions of fairness (figure 3.14) and may matter more than absolute salaries in determining levels of corruption. If this is true, increasing judges' salaries will have little effect without also paying attention to the drivers of salaries for private lawyers, including demand for services, supply constraints, and other market imperfections.

Credibility

The last aspect of court performance examined in this section is the ability of the courts to enforce decisions and the overall credibility of contract enforcement. Figure 3.7 showed that for a hypothetical business case—collecting on a debt—the time it takes post-trial to enforce the decision can be significant, ranging from 30 to 360 days. It takes more than four months to enforce a decision in 15 transition countries. Indeed, in a few countries the time it takes to get the decision enforced is longer than either the pre-trial or trial phases of collection. Figure 3.15 shows how firms assessed the ability of courts to enforce decisions in both 1999 and 2002. Again, for the transition countries as a whole, the perceptions of firms were more negative in 2002 than three years earlier. Only four countries—Albania, Belarus, Latvia, and Ukraine—showed significant improvement, while Bulgaria, Georgia, Romania, the Slovak Republic, Slovenia, and Uzbekistan showed a significant decline. Fewer than half of firms in almost all transition countries surveyed in 2002 believed that courts were able to enforce their decisions.

The Doing Business database helps illustrate the links between the ability of courts to enforce decisions, aspects of court efficiency, and the

Figure 3.13 Unofficial payments and gifts when dealing with courts, 1999 and 2002

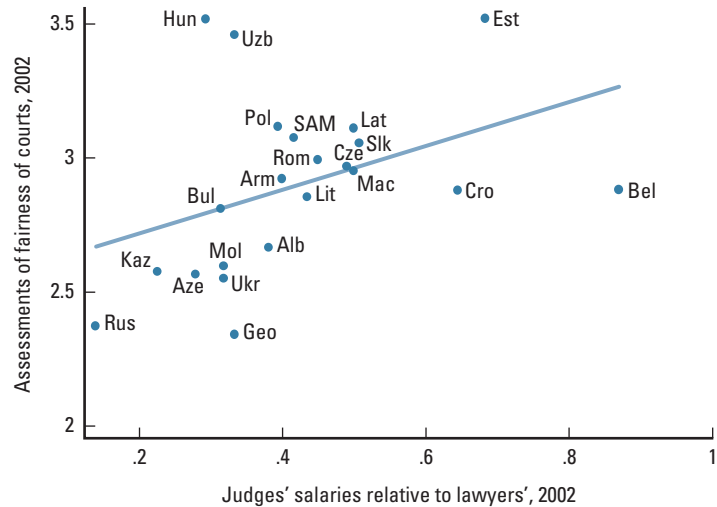


Sources: BEEPS1; BEEPS2.

Note: See appendix 3 for details. 1=never...6=always. SAM and Tajikistan not surveyed in 1999. Changes statistically significant for Albania, Armenia, Azerbaijan, Belarus, Bosnia and Herzegovina, Hungary, Kyrgyz Republic, Lithuania, Moldova, Poland, Romania, the Russian Federation, Ukraine, and Uzbekistan.

problems that inefficiency in the judiciary poses for firms. Figure 3.16 shows the Doing Business index capturing the complexity of enforcing a contract plotted against an index of the degree to which contract violations are a problem for firms, taken from the BEEPS data. Where

Figure 3.14 Do judges' salaries relative to lawyers' salaries affect the fairness of courts?



Sources: BEEPS2; EBRD Legal Indicator Survey.

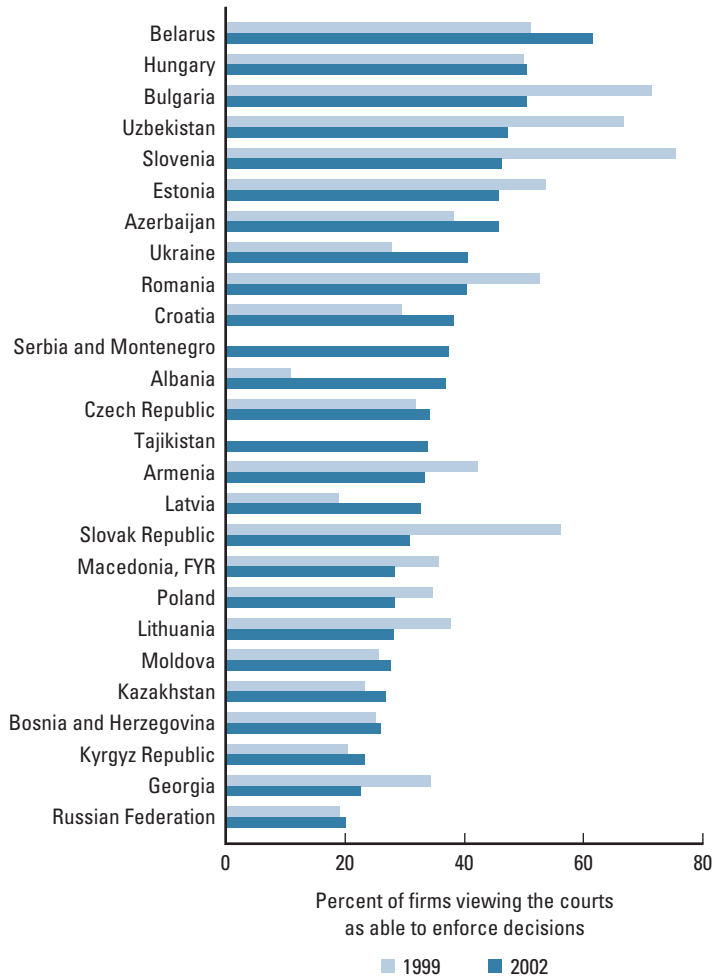
Note: See appendix 3 for details. Alb = Albania; Arm = Armenia; Aze = Azerbaijan; Bel = Belarus; Bul = Bulgaria; BiH = Bosnia and Herzegovina; Cro = Croatia; Cze = Czech Republic; Est = Estonia; Geo = Georgia; Hun = Hungary; Kaz = Kazakhstan; Kyr = Kyrgyz Republic; Lat = Latvia; Lit = Lithuania; Mac = Macedonia, FYR; Mol = Moldova; Pol = Poland; Rom = Romania; Rus = Russian Federation; SAM = Serbia and Montenegro; Slk = Slovak Republic; Sln = Slovenia; Taj = Tajikistan; Ukr = Ukraine; Uzb = Uzbekistan.

enforcing a contract through the courts is complex, we see that more firms identify contract enforcement as a problem for their operations. These firms are more likely to seek alternatives to judicial enforcement in their contractual relations. Contract violations, in turn, may lead to economically less efficient outcomes, such as relational contracting, reliance on “private enforcement,” or barter.

Understanding the linkages among reforms

The many and varied types of reforms needed during the transition cannot be considered in isolation. Just as reforms in the social sectors may have important macroeconomic implications, a wide range of market reforms undertaken over the past 15 years has also opened the

Figure 3.15 Assessments of courts as “able to enforce decisions,” 1999 and 2002



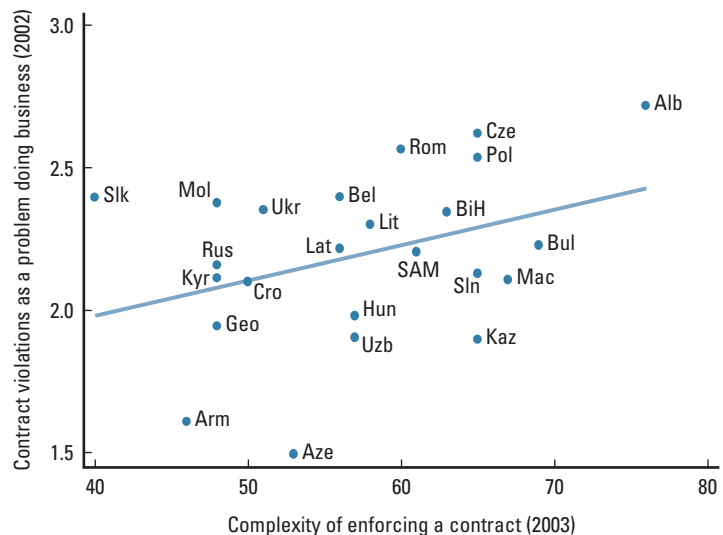
Sources: BEEPS1; BEEPS2.
 Note: See appendix 3 for details. Serbia and Montenegro (SAM) and Tajikistan were not surveyed in 1999. Changes statistically significant for Albania, Belarus, Bulgaria, Georgia, Latvia, Poland, Romania, Slovak Republic, Slovenia, Ukraine, and Uzbekistan.

door for new forms of disputes and can increase pressure on court systems originally designed to handle only criminal and family law matters. For example, privatization processes, particularly those involving restitution, have inevitably led to an increase in disputes in and out of

court. Similarly, resettlement of refugees has been a divisive legal issue in post-conflict areas, in particular in Bosnia and Herzegovina, and disputes related to newly established private property—such as conflicting claims to apartments—have increased pressure on the courts.

Figure 3.17 shows that countries that have proceeded the farthest in reforms, as measured by the EBRD’s Transition Indicators, tend to have larger fractions of firms that have been involved in court cases, as measured by the BEEPS. These include strong reformers in the 1990s such as Lithuania and Poland, as well as countries that have increased their pace of reform more recently, such as Bulgaria, Romania, and the countries of the former Yugoslavia. Yet even though both the pace of reforms and the use of courts are significant in many transition countries, further progress is needed on both fronts. Several studies have made the link between financial sector depth, corporate governance, and the

Figure 3.16 Procedural complexity and the effect on firms



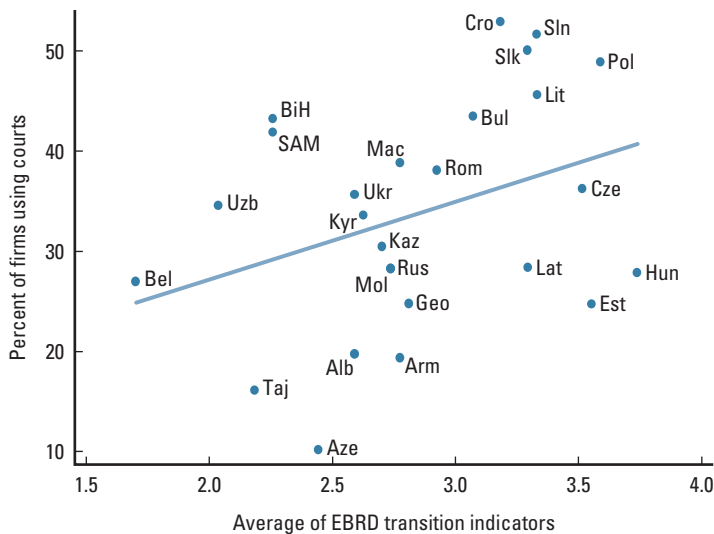
Sources: BEEPS2; Doing Business database, 2003.

Note: See appendix 3 for details. Alb = Albania; Arm = Armenia; Aze = Azerbaijan; Bel = Belarus; Bul = Bulgaria; BiH = Bosnia and Herzegovina; Cro = Croatia; Cze = Czech Republic; Est = Estonia; Geo = Georgia; Hun = Hungary; Kaz = Kazakhstan; Kyr = Kyrgyz Republic; Lat = Latvia; Lit = Lithuania; Mac = Macedonia, FYR; Mol = Moldova; Pol = Poland; Rom = Romania; Rus = Russian Federation; Slk = Slovak Republic; Sln = Slovenia; Taj = Tajikistan; Ukr = Ukraine; Uzb = Uzbekistan. Contract violations: 1 = no obstacle...4 = major obstacle.

functioning of the legal and judicial system.¹¹ The widespread reliance on retained earnings and relative paucity of sales on credit in many countries are often taken as indirect indicators of confidence in the courts.¹² A reliance on barter can also result from weaknesses in the judiciary and resulting difficulties collecting from debtors.

In countries where firms use courts more extensively, firms are also less likely to rate their courts as “quick,” as shown in figure 3.18. In the South Caucasus, for example, the relatively positive ratings for the speed of the courts may be influenced in part by the fact that relatively fewer firms say they use the courts than in other countries. Furthermore, in countries where courts are used less often, firms report courts to be less of a problem (figure 3.19). Thus there is a complex relationship between use and perception of the courts, with greater reliance, even if useful, not necessarily leading to better perceptions.¹³

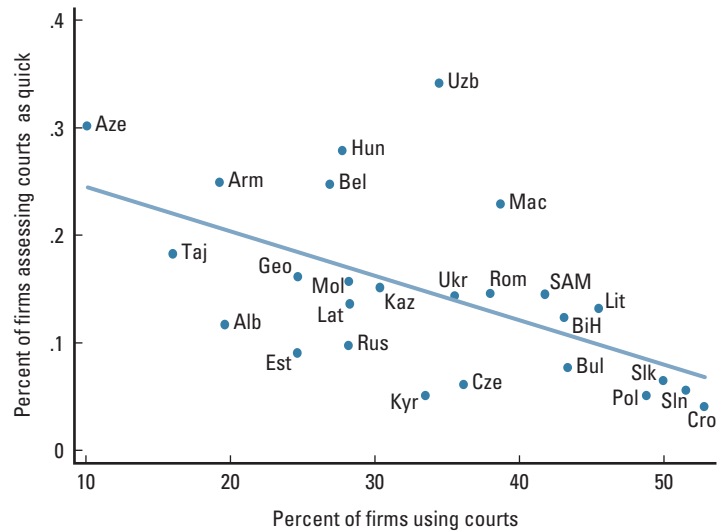
Figure 3.17 Reforms increase pressure on courts, 2002



Sources: BEEPS2; EBRD Transition Report 2002.

Note: See appendix 3 for details. Alb = Albania; Arm = Armenia; Aze = Azerbaijan; Bel = Belarus; Bul = Bulgaria; BiH = Bosnia and Herzegovina; Cro = Croatia; Cze = Czech Republic; Est = Estonia; Geo = Georgia; Hun = Hungary; Kaz = Kazakhstan; Kyr = Kyrgyz Republic; Lat = Latvia; Lit = Lithuania; Mac = Macedonia, FYR; Mol = Moldova; Pol = Poland; Rom = Romania; Rus = Russian Federation; Slk = Slovak Republic; Sln = Slovenia; Taj = Tajikistan; Ukr = Ukraine; Uzb = Uzbekistan.

Figure 3.18 Pressure on the courts slows them down, 2002



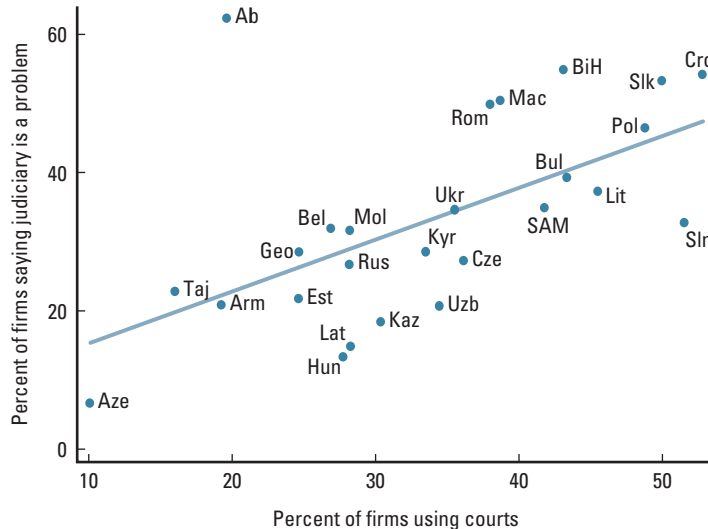
Source: BEEPS2.

Note: See appendix 3 for details. Alb = Albania; Arm = Armenia; Aze = Azerbaijan; Bel = Belarus; Bul = Bulgaria; BiH = Bosnia and Herzegovina; Cro = Croatia; Cze = Czech Republic; Est = Estonia; Geo = Georgia; Hun = Hungary; Kaz = Kazakhstan; Kyr = Kyrgyz Republic; Lat = Latvia; Lit = Lithuania; Mac = Macedonia, FYR; Mol = Moldova; Pol = Poland; Rom = Romania; Rus = Russian Federation; Slk = Slovak Republic; Sln = Slovenia; Taj = Tajikistan; Ukr = Ukraine; Uzb = Uzbekistan.

What makes courts problematic for firms?

A simple and straightforward summary measure of the condition of the judiciary is the degree to which firms believe that the functioning of the judiciary is a problem for doing business. This measure is not without ambiguity—firms are less likely to report courts as a problem if courts are not regularly used, for example—but its simplicity makes it a useful measure of how firms feel about the state of the judiciary. Figure 3.20 shows the percentage of firms in both 1999 and 2002 that reported the functioning of the judiciary to be a problem. Judiciaries in southeastern Europe (including Albania, Bosnia and Herzegovina, Bulgaria, Croatia, FYR Macedonia, Romania, and Serbia and Montenegro) tend to be seen as most problematic, while those in the CIS and EU accession countries (other than Lithuania, Poland, and the Slovak Republic) are perceived by

Figure 3.19 Courts are viewed as less problematic where they are less relevant, 2002



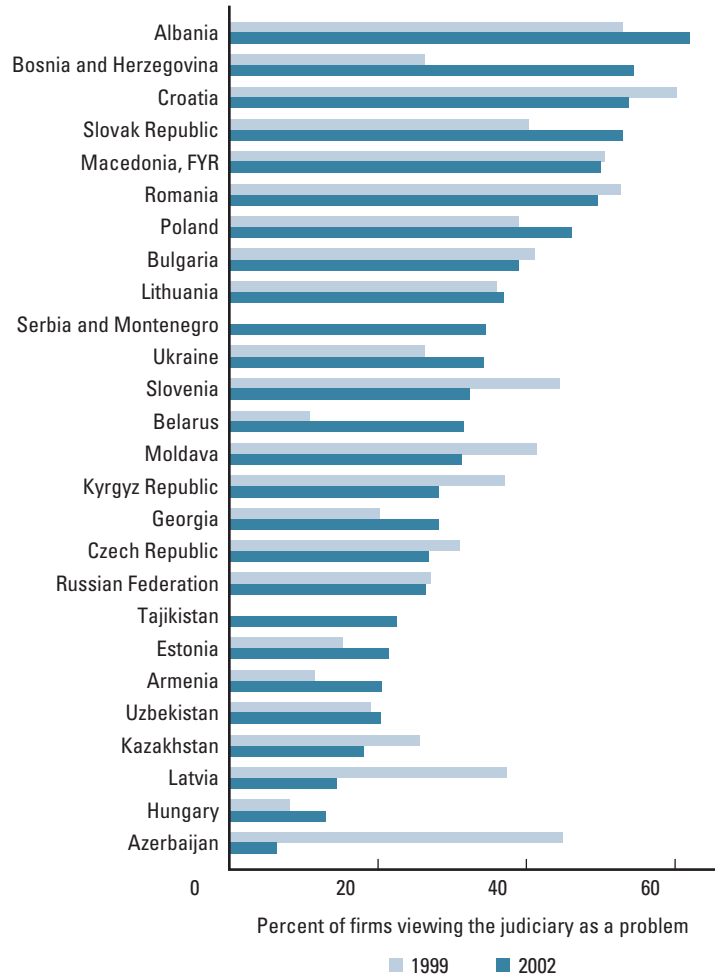
Source: BEEPS2.

Note: See appendix 3 for details. Alb = Albania; Arm = Armenia; Aze = Azerbaijan; Bel = Belarus; Bul = Bulgaria; BiH = Bosnia and Herzegovina; Cro = Croatia; Cze = Czech Republic; Est = Estonia; Geo = Georgia; Hun = Hungary; Kaz = Kazakhstan; Kyr = Kyrgyz Republic; Lat = Latvia; Lit = Lithuania; Mac = Macedonia, FYR; Mol = Moldova; Pol = Poland; Rom = Romania; Rus = Russian Federation; Slk = Slovak Republic; Sln = Slovenia; Taj = Tajikistan; Ukr = Ukraine; Uzb = Uzbekistan.

business as less of a problem. Figure 3.21 shows the percentage for 2002 and compares this to the average percentage of firms rating other aspects of the business environment (such as taxes, financing, inflation, and regulations) as problematic. While many firms view the functioning of the judiciary as a problem for their operations, for transition countries—with the notable exception of most countries in southeastern Europe—other problems appear to be even more severe. As noted in chapter 1, however, indicators for the judiciary seem to be getting worse in many countries, while indicators in other areas appear to be improving.

Understanding what firms have in mind when they complain about courts can help to identify reforms that are likely to lead to the strongest improvements in performance, at least from the firm's perspective. Firms that participated in the BEEPS surveys were asked to provide assessments of four dimensions of court performance: fairness and honesty,

Figure 3.20 Functioning of the judiciary as a problem doing business, 1999 and 2002



Sources: BEEPS1; BEEPS2.

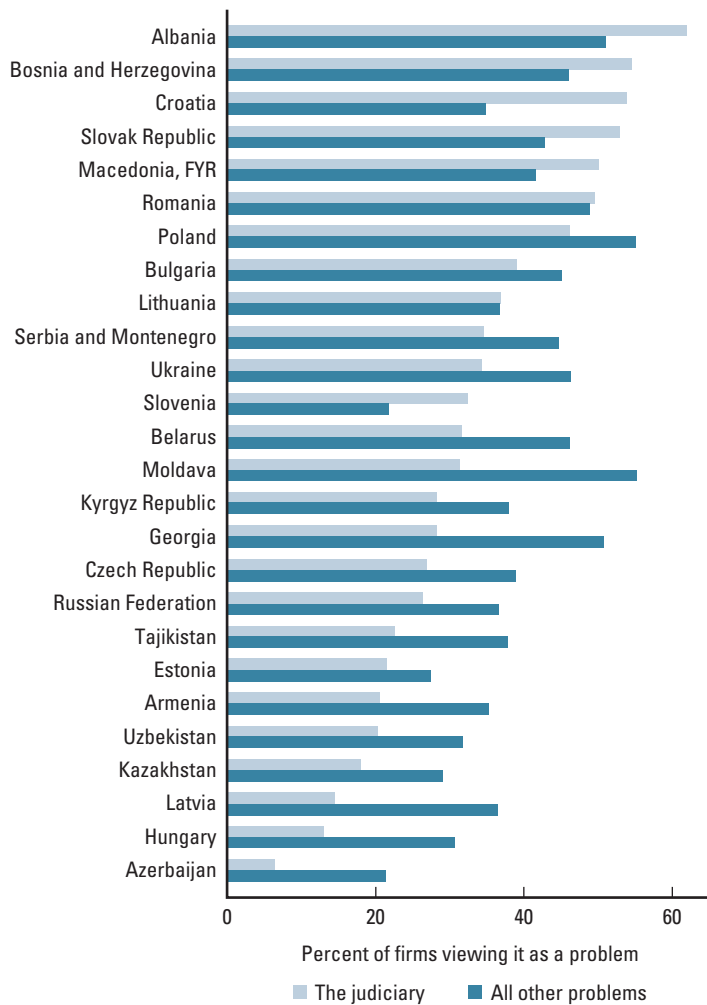
Note: See appendix 3 for details. SAM and Tajikistan were not surveyed in 1999. Changes statistically significant in Armenia, Azerbaijan, Belarus, Bosnia and Herzegovina, Latvia, Moldova, Poland, Romania, Slovak Republic, Slovenia, and Ukraine.

speed, affordability, and ability to enforce decisions.¹⁴ Similarly, firms were asked to assess how problematic “functioning of the judiciary” is for the operation and growth of the firm. By relating the overall assessment to each of the four dimensions, it is possible to get a picture of

which dimensions firms have in mind when they say that the functioning of the judiciary is a problem for their business.

As seen in figure 3.22, all four aspects of well-functioning judiciaries were important in explaining how a firm would rate “functioning of the judiciary” as a problem for the firm’s operations in 1999. The coefficient

Figure 3.21 The judiciary compared to other “problems,” 2002



Source: BEEPS2.

Note: See appendix 3 for details. Differences between bars were statistically significant in all countries except Estonia, Lithuania, and Romania.

related to speed was twice as large in absolute value, however, as the other coefficients. For 2002, by contrast, affordability ceased to be a significant variable, while the other three factors were of approximately equal importance.

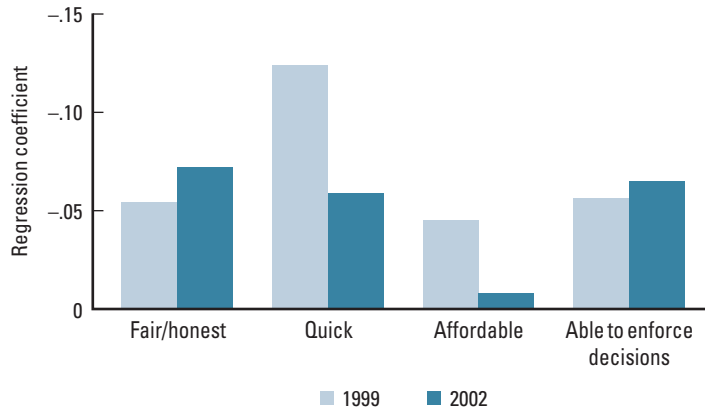
Clearly, many dimensions of court performance matter for doing business. Firms want courts that are fair and honest, strong enough to enforce their decisions, fast, and affordable. As this review has shown, however, reforms that might strengthen one dimension may weaken another. Understanding and addressing legal and judicial reform along multiple dimensions is critical for improving the functioning of the system as a whole.

Toward a typology for judicial reforms

A consistent theme of the preceding sections is the link between market reforms on the one hand and the qualities of the judiciary on the other. There are two potential aspects to this relationship. First, enterprises' need for well-functioning judiciaries and the consequent demands on the system are likely to be greater where reforms are more advanced. Advanced market reformers, such as the European Union's new members, have shifted their economies more completely toward arms-length private production. Reliance on the legal system to resolve disputes has replaced the administrative solutions of central planning, and the expanded size of the private sector has increased the number of economic transactions that could potentially lead to disputes. These increasing demands on the courts tend to slow them down, but the demands also generate further support for judicial strengthening. Businesses that increasingly rely on the judicial system have a stake in efforts to make courts fair, fast, affordable, and effective. Second, more advanced reformers tend to have higher per capita incomes and are likely to be able to provide greater capacity in the judiciary in terms of staff quality and training, buildings and other physical capital, and operating budgets. And the higher demand for judicial services reinforces the pressure to continue strengthening capacity, creating a "virtuous circle" of increasing usage and improving capacity.

Does this hypothesized virtuous circle hold in practice? Figure 3.23 shows a rudimentary typology of countries based on the two dimensions of enterprise demand for judicial services and judicial capacity. Because

Figure 3.22 Relative importance of various factors in explaining the functioning of the judiciary in transition countries, 1999 and 2002



Sources: BEEPS1; BEEPS2.

Note: See appendix 3 for details. All coefficients were statistically significant except for affordability for 2002.

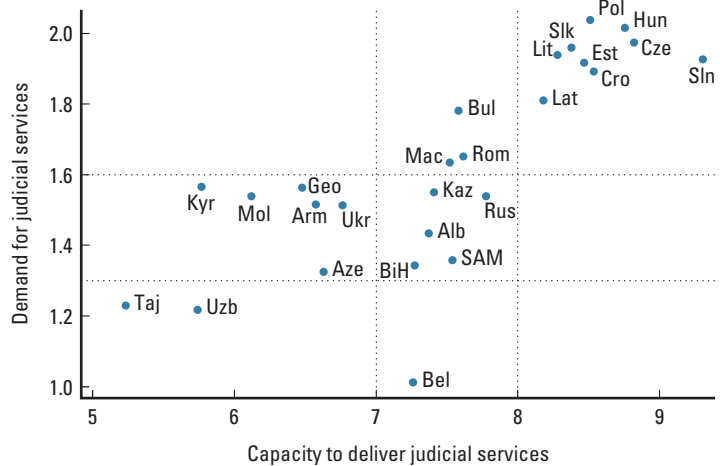
such concepts cannot be easily measured, we must use available proxies. The proxy used here for judicial capacity is the log of gross domestic product (GDP) per capita, based on the hypothesis that greater resource availability suggests stronger capacity. The proxy for demand is the average of (1) the percentage of firms that have used the courts and (2) the mean EBRD transition indicator for 2002.¹⁵ Horizontal and vertical dotted lines have been included to suggest certain rough groupings of countries.

As expected, there is a strong relationship between the extent of economic reforms and resulting demand for judicial services and judicial capacity. All eight new members of the European Union and Croatia (the country outside the EU with the highest per capita income) fall in the upper right square of the figure. A group of reforming countries with almost as strong a demand for judicial services, but somewhat lower judicial capacity, includes Bulgaria, FYR Macedonia, and Romania. Among countries with moderate demand for judicial reforms there is wide variation in capacity, with other southeastern European countries (Albania, Bosnia and Herzegovina, and Serbia and Montenegro), Kazakhstan, and Russia toward the upper end of the scale, and several

lower-income CIS countries—Georgia, the Kyrgyz Republic, and Moldova—toward the lower, again highlighting the link between capacity and per capita income. The group of countries with the lowest demand for judicial reforms includes Belarus, Tajikistan, and Uzbekistan, with the latter two also having the lowest capacity (again a function of both low income and weak demand).

Figure 3.24 revisits a key assessment of the quality of courts used throughout this report, the assessment by firms of whether the judiciary poses a problem for the operation and growth of their firms. The height of each column is the average assessment of this variable (the extent to which the judiciary is a problem) across the countries in the corresponding cell in figure 3.23. Figure 3.24 is instructive in the patterns it exposes. As discussed in the previous section of this chapter on linkages among reforms, firms in countries with low demand for judicial services report the most positive assessments of the judiciary (that is, they indicate that

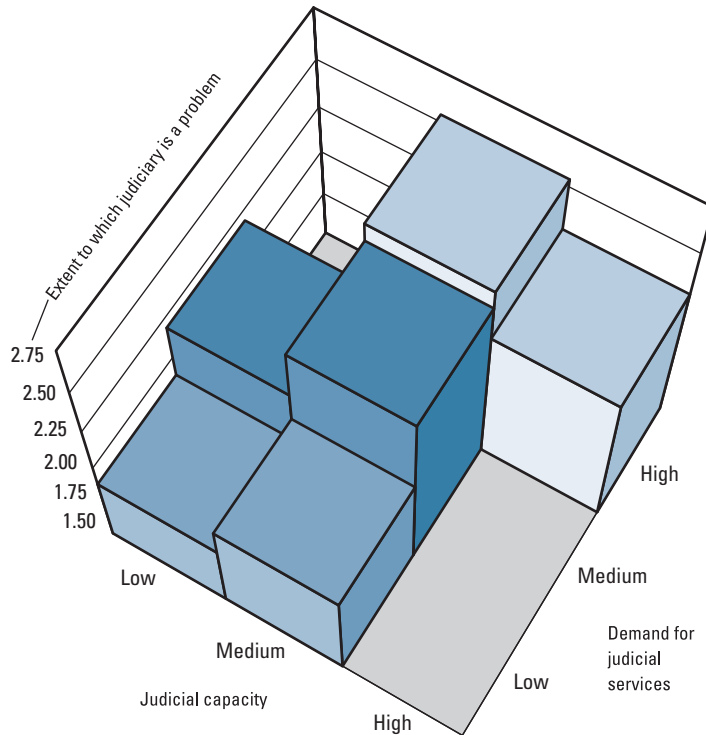
Figure 3.23 Capacity and demand for judicial services, 2002



Sources: BEEPS2; EBRD Transition Report; World Development Indicators.

Note: See appendix 3 for details. Alb = Albania; Arm = Armenia; Aze = Azerbaijan; Bel = Belarus; Bul = Bulgaria; BiH = Bosnia and Herzegovina; Cro = Croatia; Cze = Czech Republic; Est = Estonia; Geo = Georgia; Hun = Hungary; Kaz = Kazakhstan; Kyr = Kyrgyz Republic; Lat = Latvia; Lit = Lithuania; Mac = Macedonia, FYR; Mol = Moldova; Pol = Poland; Rom = Romania; Rus = Russian Federation; SAM = Serbia and Montenegro; Slk = Slovak Republic; Sln = Slovenia; Taj = Tajikistan; Ukr = Ukraine; Uzb = Uzbekistan. Capacity is the log of GDP per capita. Demand is based on court usage and the EBRD transition indicators.

Figure 3.24 The judiciary as a problem, by capacity and demand for judicial services, 2002



Sources: BEEPS2; EBRD Transition Report; World Development Indicators.
 Note: See appendix 3.

courts are the least problematic for doing business). Low capacity does not matter because the courts are simply not very relevant for most firms in those countries. Higher demand is, on average, associated with more negative assessments of the judiciary by firms, at least until capacity gets to be substantial (as in the upper right-hand cell of figure 3.23). The demand for judicial services is likely to rise more quickly than judicial capacity, given the typically slow pace of institutional reform. Thus one can expect negative public perceptions and the economic costs of poorly functioning judiciaries to increase in the early stages of transition as expectations for court performance rise, while capacity lags (as we have seen in this report). Then, if all goes well, economic costs will level off

and decrease and perceptions will improve, as reforms spur economic growth and the commercial demand spurs judicial capacity building.

Notes

1. The 14 countries covered by at least one JRI as of December 2004 are Albania, Armenia, Bosnia and Herzegovina, Bulgaria, Croatia, FYR Macedonia, Kazakhstan, the Kyrgyz Republic, Moldova, Romania, Serbia and Montenegro, the Slovak Republic, Ukraine, and Uzbekistan.
2. For the purposes of this discussion, “non-EU” refers to countries that were not members of the EU at the time of the surveys. The Czech Republic, Hungary, Poland, and the Slovak Republic became members of the EU in 2004.
3. See appendix 3 for a description of the aspects of the judiciary used in the indexes of efficiency and independence.
4. Of course, increased efficiency does not necessarily translate into more independent judges or fairer outcomes. Indeed, as noted below, firms provide low assessments for the fairness and honesty of courts in both Kazakhstan and the Kyrgyz Republic, the latter receiving the lowest ratings among transition countries.
5. For purposes of the JRI, trial records include a transcript or some other reliable record of courtroom proceedings that are available to the public.
6. The overall correlation between the 2002 BEEPS measure of court speed and the 2003 Doing Business measure of court delays is -0.44 . For some countries, the assessments of courts by firms in the BEEPS are very much congruent with the Doing Business data. Azerbaijan and Uzbekistan, for example, are the two countries with the highest rating for speed in figure 3.6, and they also have fairly small time delays for pre-trial and trial phases in the 2003 and 2004 versions of Doing Business.
7. Dietrich 2000.
8. The results for Armenia may be attributable to the fact that the period of 1997–9 saw dramatic changes in the organization and authority structure of Armenia’s judicial system, so courts were still in transition from the Soviet model when firms were surveyed in 1999. A survey concluded in early 2000 for the World Bank’s Judicial Reform Project found that only 2 percent of those surveyed viewed judges as honest, and experts felt the existing system was corrupt. (See Center of Ethnosociological Studies 2000). The improvement in Armenian firms’ perceptions in 2002 must be measured from this low starting point.
9. It would be helpful to benchmark these findings against similar data from more advanced market economies, but unfortunately very little

data on this topic exist in the latter. The small amount of comparable data that exists supports the view that judicial corruption is more widespread in the transition countries. (See, for example, the 2003/2004 survey comparing citizens' perceptions of corruption in Austria and 13 European transition countries, available at <http://www.gfk.cz>.)

10. This is not the only area where reported levels of corruption appear to have declined between 1999 and 2002. For more in-depth analysis of changes in reported levels of corruption in transition economies during this period, see Gray, Hellman, and Ryterman (2004).
11. Examples include: Beck and Levine 2003; Pistor, Raiser, and Gelfer 2000; and La Porta, Lopez-de-Salines, and Schleifer 1997.
12. This point is illustrated for southeast Europe, for example, in Broadman, Anderson, Claessens, Ryterman, Slavova, Vagliasindi, and Vincelette (2004).
13. The complex relationship between firm perceptions of the qualities of the courts, their use of courts, and the influence of market reforms is examined in further depth in appendix 3. The main story told by the bivariate relationships presented above is generally supported by more in-depth statistical analysis.
14. Of the five dimensions described in this paper, fairness and honesty were conceptually very similar to each other and were aggregated to construct an index. Thus, the four dimensions considered for the present exercise were fairness and honesty, speed, affordability, and ability to enforce decisions.
15. Such a typology is, of course, highly imperfect. The variables are only rough approximations of the concepts we are trying to measure, and the variables themselves are measured imperfectly. Furthermore, the placement of indicative dividing lines is necessarily arbitrary. The goal is to see if certain groupings of countries emerge that suggest that different reform priorities and approaches may be warranted given current circumstances.

4

Conclusion: Lessons for Future Reform

THE ANALYSIS IN THIS REPORT SHOWS A MIXED PICTURE WITH REGARD to progress made on legal and judicial reform in the transition countries since the early 1990s. On the one hand, significant progress has been achieved in a number of countries in a number of areas, including independence, increased judicial training capacity, and initial steps toward judicial self-regulation and management of court administration. However, as many surveys and expert analyses show, much remains to be done to increase the capacity of both judges and their staff, reduce case backlogs and increase court efficiency, develop the proper incentives and deterrence to address both the perception and the reality of corruption in the region's judiciaries, and promote greater access to the courts. Along many important dimensions of performance that matter to investors and citizens alike—including affordability, fairness, speed, and ability to enforce decisions—courts in many transition countries appear to have deteriorated rather than improved in recent years. Indeed, it is probably fair to say that less overall progress has been made in judicial reform and strengthening than in almost any other area of policy or institutional reform in transition countries since 1990.

General lessons

While each country presents different challenges and opportunities, certain lessons apply in most settings:

- **Complement Structural Independence with Operational Independence:** Efforts at building a depoliticized and independent judiciary in

the transition countries have focused so far primarily on formal, structural independence, neglecting (until recently in a few countries) reforms that would make judiciaries operationally independent from Ministries of Justice. For example, while judicial councils or judicial administration bodies have been created in many countries, these bodies have not been given full authority or the necessary capacity to manage the judiciary, including overseeing or at least influencing staffing, budgeting, and disciplinary proceedings.¹ Assistance to help clarify the roles and responsibilities of judicial administrative bodies and capacity-building programs that provide these self-management bodies with authority, resources, and staff would go a long way to help courts operate effectively and efficiently.

- **Link Increased Independence with Strong Accountability:** Independence and accountability must go hand-in-hand to ensure honesty and quality in the judiciary. Merit-based and transparent appointment of judges, random assignment of cases, full publication and dissemination of judicial decisions, peer evaluation and oversight panels to review promotions or complaints, and strong mechanisms for citizen and media feedback on judicial performance are some of the tools that can be used to enhance judicial accountability and honesty. Given the political and technical complexities surrounding this area of reform, strong leadership and commitment from top government officials and senior judges are essential. In systems where corruption is prevalent, a major change in leadership and personnel may be required. A push for accountability should be a central pillar of judicial strengthening programs.
- **Improve Efficiency:** An additional benefit of operational independence can be improved management and more efficient functioning of the courts. The early inattention to judicial reform, particularly the lack of institution building, created a backlog of cases in nearly all the courts in the region. This backlog and the speed with which courts can dispose of a dispute directly affect firms' and investors' trust in the judicial system. Some countries have taken steps to improve the efficiency of their court systems by introducing specialized courts or specialized divisions within courts, revising procedures to reduce opportunities for parties to delay, increasing the ability of judges to control the pace of proceedings, and removing the many nonjudicial responsibilities with which many judges are saddled (such as respon-

sibility for registering pledges, probating wills, reviewing incorporation documents, or holding a hearing on all challenges to actions by administrative agencies). Replicating these and other efficiency-enhancing steps should be a priority for the next generation of legal and judicial reforms.

- **Follow-up on Lawmaking with Implementation and Enforcement:** A key lesson from the first 10 years of reform is the need to put resources and emphasis on the implementation and enforcement of legal reforms, whether through the courts or through other enforcement bodies (including company and collateral registries, notaries, bailiffs, bankruptcy trustees, land cadastres, the police, and prosecutors offices), if the legal reforms are to have real impact. Laws and regulations that are poorly enforced or not enforced at all provide little benefit to businesses and individuals seeking to invest and work in the transition economies. Closing this “implementation gap” should be an important objective of the next generation of institutional reforms in the public sector. This will require an increase in resources and a longer-term view for donors and reformers alike, as building or strengthening enforcement institutions requires time and effort.
- **Take a Broad View of Legal and Judicial Reform:** Reformers need to recognize how seemingly unrelated reforms can affect the courts and judiciary. For example, granting new rights to citizens to sue without a concomitant increase in the capacity of judges to understand and courts to handle new disputes can create logjams. Frequent changes in legislation and regulations through a closed and nontransparent legislative drafting process can leave users of the new laws confused and judges incapable of effectively interpreting and applying the new laws. The judiciary should also be seen as part of the broader legal profession—a profession with a limited stock of human capital and one facing competition for resources and salaries as economic growth and investment take hold. Therefore, reforms should consider the incentives facing legal professionals within and outside the judiciary as well as the constraints on entry and exit in the market for legal services. It is important to keep judges’ salaries reasonable in light of the salaries of private lawyers and other related professions, and to permit ready entry into the legal profession to allow competitive forces to operate to maintain quality without exorbitant increases in cost.

■ **The Importance of Process and the Impact of Donor Influences:**

Donor preferences and pressures to reform have had a significant impact on the shape and operation of judicial systems in transition countries. Recognizing this impact, donors such as the World Bank, the European Union, and bilateral assistance agencies need to work collaboratively with governments to ensure that reforms reflect local needs and capacities. In addition, an emphasis on the *process* of reform (including the process of legislative and regulatory drafting and review and the process of policy formulation for the judiciary) should be a focus of future reform efforts to improve the sustainability of the overall transition process.

Setting priorities

While the general lessons outlined above apply in most settings, the analysis in this report also shows that transition countries differ significantly among themselves, not only in the specific problems they face, but also in both judicial capacity and in the public “demand” for well-functioning judiciaries. Both demand and capacity—at least in the economic sphere—are, in turn, related to the extent of economic reform and the per capita income in the country concerned. The typology in chapter 3 places transition countries along these two dimensions of judicial capacity and enterprise demand for judicial services. The strategy and priorities for each country going forward will depend on what its particular problems are and where it lies in the typology presented in figure 3.24, above.

Weak demand: focus on fundamental economic reforms

In countries where businesses’ demand for well-functioning judiciaries is relatively weak (Belarus, Tajikistan, and Uzbekistan), judicial reform and capacity strengthening should arguably not have high priority, given the inevitable scarcity of resources. Firms will provide little real pressure for reform, and reforms, once enacted, will be prone to weak implementation or backsliding. A judicial strategy in such an environment should focus on building basic demand for impartial dispute resolution through continued market reforms. As a private sector and enhanced demand for judicial services begin to emerge, emphasis can increasingly be placed

on building greater independence, accountability, and legitimacy in the courts, while gradually strengthening their capacity.

Moderate demand: continued economic reforms and judicial strengthening

Countries that are further along on the economic reform path face a more complex challenge. The demand for judicial reforms has strengthened, which both puts the spotlight on problems of judicial capacity and suggests that further reforms and capacity building are worth the effort and may be sustainable. In this situation the question of priorities and sequencing is often center-stage.

If capacity is relatively weak, as the typology suggests for several low-income countries in Central Asia and the Caucasus, enthusiasm for complex reforms should be tempered by the reminder of the low capability of such countries to implement reforms. Top priorities for action are likely to include continued structural reforms—including efforts to enhance independence and accountability—and basic investment in capacity, such as testing of judges to weed out gross incompetence, refurbishing selected court buildings to provide functional space, providing simple IT infrastructure to allow sharing of information and increased transparency, and allowing courts to hire clerks or administrators to free-up the time of judges. Deepening market reforms will maintain a level of prominence on the judicial reform agenda, but will share this space with targeted efforts to build accountability mechanisms and improve the capacity and legitimacy of the judiciary.

Countries with moderate levels of both demand and capacity have clearly demonstrated the relevance of the courts and have substantial private sectors with large stakes in the continuation of improvements to the judiciary. For these countries, the capacity for more advanced reforms exists, and the moderate levels of demand suggest that pressure will help to ensure that reforms take hold. In such environments, judicial strategies may focus on balanced strengthening of many—and often more complex—aspects of court performance, including efficiency, honesty, accessibility, and affordability, and capacity to enforce decisions. The moderate demand for reforms, however, does not guarantee against backsliding, and continued attention to market reforms should still play an important role in such environments.

Strong demand: from comprehensive to focused judicial reform

As shown in figure 3.24, above, firms in countries with strong demand for judicial services yet only moderate judicial capacity have the most negative view of the judiciary as a problem for the growth and operation of their businesses. Three countries—Bulgaria, FYR Macedonia, and Romania—fall into this category in our typology. Bulgaria and Romania are both scheduled to join the European Union in 2007, and FYR Macedonia is awaiting an EU decision and timetable for its eventual accession. All three countries have substantial private sectors with a strong need for more effective legal and judicial systems, and EU reports routinely emphasize the need for judicial strengthening. All three also have reform-oriented governments that recognize the acute need for change and have put judicial reform as a top priority. Comprehensive judicial reform strategies addressing all aspects of reform—independence, accountability, court efficiency and performance, access and affordability, alternative dispute resolution mechanisms, and the design and functioning of related professions (such as the bar, bailiffs, and notaries)—are appropriate in these settings.

Finally, the countries with both high demand and high capacity—the new EU members and Croatia—are in a relatively enviable position. Most have already accomplished the basic reforms and can focus on remaining areas of weakness. The key constraints tend to be more specific and easier to identify in these countries.² Our analysis suggests, for example, that areas of needed emphasis may be speed in the Slovak Republic, ability to enforce decisions in Poland and the Baltics, and fairness and honesty in Hungary.

This report has pulled together a wide variety of sources of data and analyses to describe the judicial systems in operation in the transition countries a decade and a half after the fall of the Berlin Wall. The purposes of the analysis were to illuminate differences and commonalities among countries with regard to the need for reform and the stage of reform, as well as to suggest priorities for further action. Further country-specific diagnostic surveys and more in-depth analysis of specific issues would help to refine priorities further and set the course and enhance the impact and sustainability of future reform efforts.

The underlying message is the critical importance of judicial strengthening to the transition process. Rule of law is essential to a well-

functioning market economy, and leaders in many transition countries see the need to develop effective, efficient, and credible legal and judicial systems as among their highest priorities. We hope that the analysis and lessons in this report can help to guide the work going forward.

Notes

1. One recent exception to this situation is FYR Macedonia, where the Judicial Budget Council was given authority over the budget for the judicial system. Donors are helping the Council build the structures and capacity necessary to exercise this authority.
2. Chapter 3 included an analysis of what firms mean when they report that the courts are problematic, and the results were presented in figure 3.22. A similar set of regressions was run for each country individually in an attempt to understand what aspects of the courts were associated with overall performance from the perspective of firms. Interestingly, the ability of the model to explain firms' assessments of the judiciary as a problem doing business was closely related to where a country fell in the typology of figure 3.23. The further from the origin, that is the higher the capacity and demand for judicial services, the more likely it is that assessments of the courts are related to specific aspects of court performance, rather than being a reflection of general distrust. See appendix 3 for details.

Appendices

APPENDIX I

Turkey—A Different Path For Legal and Judicial Reform

The Europe and Central Asia (ECA) region in the World Bank comprises all former socialist countries in CEE and the CIS as well as Turkey. Turkey was not included in the analyses in the body of this report because of its very different history, having never been part of the communist world. With a population of 70 million people, however, Turkey is the second largest country in the ECA region. This appendix summarizes its legal and judicial reforms and compares its indicators with those of other ECA countries for readers who are interested in comparative analysis.¹

The foundation of the modern legal and judicial system in Turkey was formed when the Shariah Courts were replaced with secular courts in accordance with the Judicial Organization Law passed shortly after the Republic was established in 1923, although the genesis of the secularization began decades earlier. The *Hatt-i Sherif*, considered one of the most important documents in modern Middle Eastern history, was written in 1839 by the Foreign Minister of the Ottoman Empire and includes an important affirmation of the rule of law: the declaration that laws must apply equally to all subjects, both Muslim and non-Muslim. Reform during the 19th century led to the creation of dual judicial systems with shariah and secular courts existing side-by-side.

The modernization of the legal system that began in the 1920s drew heavily on continental approaches: the Turkish legal system was based on Swiss civil law and civil procedure; German commercial law, maritime law, and criminal procedure; Italian criminal law; and French

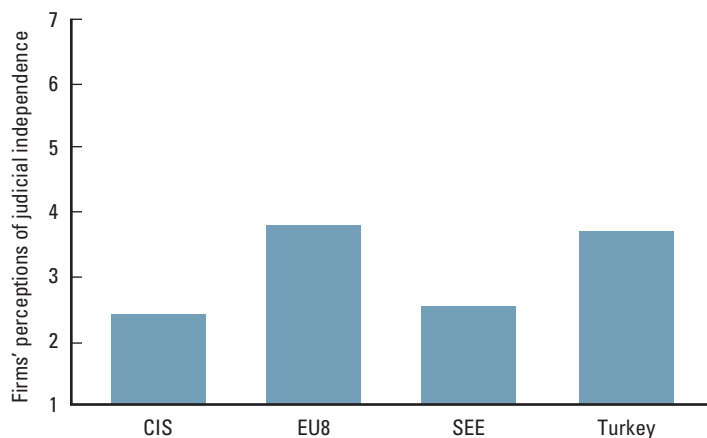
administrative law. The different codes were chosen from what were considered to be the best in the field for various reasons, including prestige, efficiency, and chance. Choosing a number of different models may have given the borrowings “cultural legitimacy,” in that the push to modernize and westernize would not be tied to any one dominant culture. The goal behind using foreign laws was to uproot the foundations of the old legal system by creating completely new laws. Importantly, these models were chosen by Turkey, not imposed, and then adapted and adjusted to fit the Turkish situation, often by Turkish academics trained in the universities of the model countries.

According to the European Union’s 2003 and 2004 Regular Reports, the main problem facing the Turkish legal and judicial system is the large backlog of cases and general inefficiency of the justice system.² The ruling Justice and Development Party has acknowledged that the running of the legal system in Turkey has been slow and ineffective and that the problem is more one of inefficient implementation than the legislation itself. The system has also been criticized for the *de facto* lack of independence of judges, despite the *de jure* commitment to independence. The reform objectives set out in the EU Accession Partnership with Turkey emphasize strengthening the independence and efficiency of the judiciary, among other goals.

At the same time, progress is being made on a number of fronts. The number of judges and prosecutors has expanded, and a new IT program enabling speedy exchange of information has continued to progress. Present reforms are geared both toward the immediate expansion of human capital through training sessions for judges and prosecutors on a wide range of issues and on institutionalizing human capital development by creating an academy to provide continuing legal training to judges, public prosecutors, and other court personnel. The EU and the World Bank are providing assistance aimed at improving information and training and strengthening the caseload management and court administration system, among other goals.

Although the perceptions of firms generally support the need to improve efficiency and independence, the perceptions of Turkish firms are not out of line with those of firms in the eight transition countries that have joined the European Union (EU8)—Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Slovenia, and Slovak Republic. Assessments of judicial independence from the EOS database are in line with those of the EU8 (figure A1.1), though neither is particularly high, while the BEEPS suggests the same for the speed of court proceedings [that is, assessments in Turkey and EU8 are similarly unfavorable, (figure A1.2)]. With regard

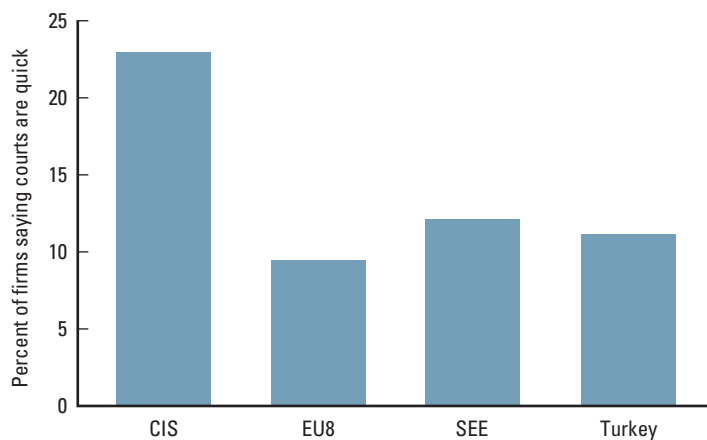
Figure A1.1 Judicial independence



Sources: Executive Opinion Survey, 2003/4.

Note: See appendix 3 for details. 1=not independent...7=completely independent.

Figure A1.2 Speed of court proceedings

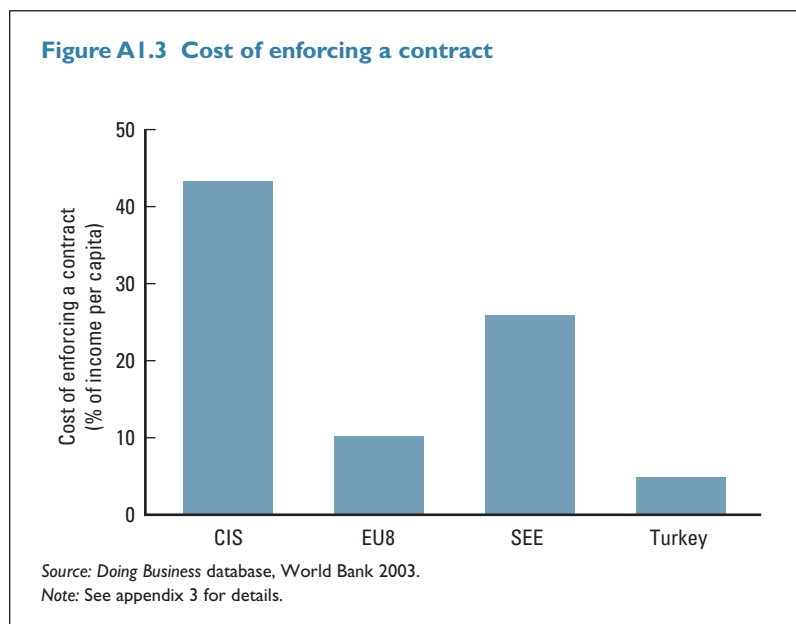


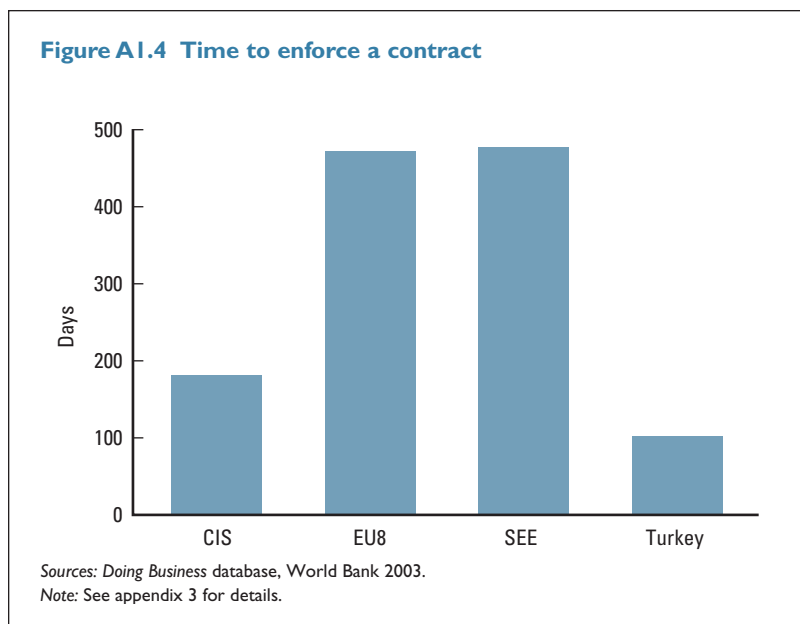
Source: BEEPS2.

Note: See appendix 3 for details.

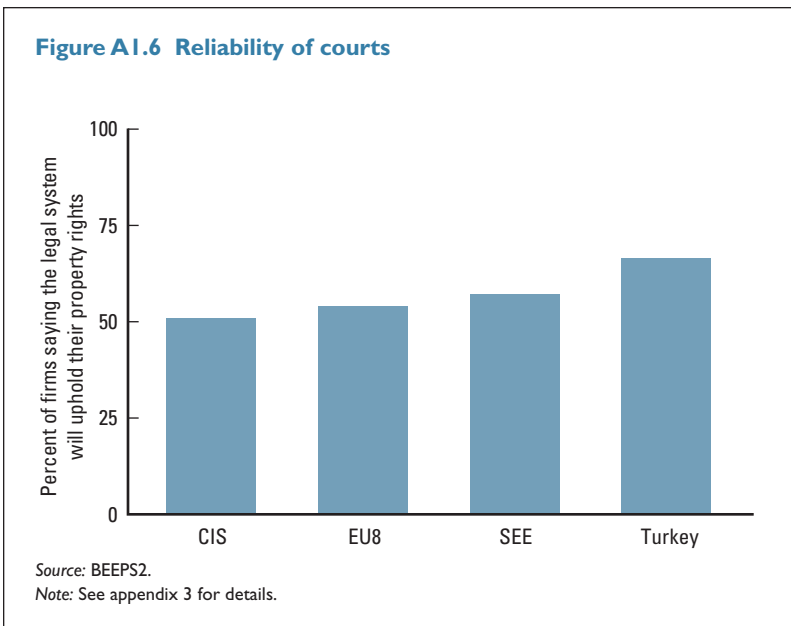
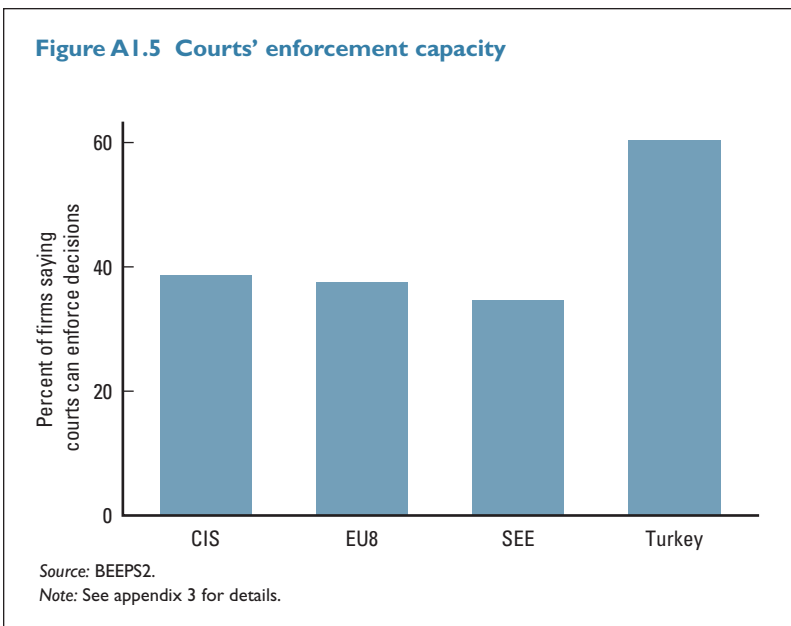
to efficiency, data from the Doing Business database supports the notion that Turkish courts perform as well or better than its EU8 counterparts. For both the cost of enforcing a contract and the length of time it takes to enforce a contract, Turkey outperforms the EU8 (figures A1.3 and A1.4).

One area where the experience of firms in Turkey is different from that of most transition countries, and especially the EU8, is that Turkish firms are much less likely to actually use the courts. In the BEEPS questionnaire, for example, firms were asked if they had been to court in the previous two years. Firms in Turkey were less than half as likely as firms in the EU8 to say they had used the courts. A second, and perhaps related, difference between the perceptions of firms in Turkey and those of firms in the EU8, is that Turkish firms provided significantly worse assessments of the courts in terms of honesty and fairness. This finding corresponds with the assessment of the Turkish Industrialists and Businessmen's Association that Turkish courts are subject to outside influences.





In terms of the actual effectiveness of the courts, firms provide more positive assessments. Turkey appears different from the EU8 and other transition countries in two important respects. First, the judicial system is viewed as stronger in Turkey in its ability to enforce court decisions (figure A1.5) and this enforcement process is cheaper and takes less time than it does in the transition countries. Second, firms in Turkey are more likely to express confidence that the legal system will uphold their rights in property disputes (figure A1.6). The greater stability of legal institutions and longer experience with market mechanisms in Turkey may help to explain these positive assessments.



APPENDIX 2

The World Bank's Support for Judicial Reform in Transition Economies

(As of early 2005)

In the earliest stages of transition in the first half of the 1990s, the World Bank focused its efforts in CEE and the CIS on laying the basic groundwork for a market economy through macroeconomic stabilization, privatization, and fiscal and banking reform. In the legal sphere, the Bank focused on helping support the drafting of specific pieces of legislation related to, *inter alia*, transportation, telecommunications, privatization, and bankruptcy, but it did not provide direct assistance to legal or judicial institutions.

The Bank's first project in direct support of legal institution-building in this region was a 1996 loan for \$58 million to Russia to support initiatives in legislative drafting, legal information, public and legal education, and judicial reform, including alternative dispute resolution. The primary justification for the Russia project was that economic reform would not flourish and private investors and entrepreneurs would not prosper without a legal system that protected private property, defended economic rights, and provided a secure environment for investment and market relations. The Bank's work in this area would help provide the legislative framework needed to support a free market economy, build the institutions necessary to interpret and enforce such laws, and attack the corruption that continued to undermine economic development. This rationale set the tone and justification for continued work in this area. The Russia project was an investment loan—that is, a loan that funds certain carefully defined activities directly.

Numerous stand-alone investment projects to support the reform of legal and judicial institutions in transition countries followed the Russian loan:

- In 1999, a \$13.4 million credit to Georgia was approved to modernize court administration and case management procedures, rebuild courthouses, assist with judicial training, and develop a public information and education component.
- Kazakhstan received a \$16.5 million loan in 1999, focusing primarily on legal drafting, judicial strengthening, and development of a modern legal information system. This loan was later cancelled, but the Kazakh government went on to implement many of the project components.
- In 2000, a judicial reform project for \$11.4 million was approved for Armenia, designed to provide investments in the same areas as Georgia's, with the addition of components on legal information and enforcement of judicial decisions.
- Albania received a \$9 million credit in 2000 for investments in legal education, court administration and case management systems, enforcement, judicial training, judicial inspection, and alternative dispute resolution mechanisms.
- Croatia's Court and Bankruptcy Administration Project was approved in 2001 for \$5 million. It focuses primarily on the regulatory framework and training skills for bankruptcy trustees and administrators, as well as investments in a computerized system for commercial court administration and case management.

In more recent years, the World Bank has tackled judicial reform in transition countries through adjustment lending as well as investment lending. Adjustment lending provides general financial support to a country's budget, conditioned on the adoption of certain reforms agreed with the government. Two recent adjustment loans have included conditions on judicial reform:

- The 2nd Programmatic Adjustment Loan (PAL 2) to Bulgaria, approved in 2004, focused on key structural and institutional reforms and called for anticorruption actions for the judiciary, preparation of uniform standards of service for court administrative staff, and submission of uniform criteria for the selection of magistrates and the evaluation of their performance to the National Assembly.
- The Romania Programmatic Adjustment Loan (PAL) program aims at reforming core public sector institutions and processes, including the judiciary, in support of the overarching objective of joining the Euro-

pean Union. In line with PAL conditionality, the Romanian Parliament adopted three organic laws on the judiciary, which redefined the appointment of judges, judicial career development, and court administration, and limited the Prosecutor General's powers to interfere with the judicial processes. The reform program also launched a comprehensive study on the rationalization of the court system and introduced the position of economic managers in the court, thereby relieving judges from time-consuming nonadjudicative tasks.

In addition to investment and adjustment lending, the World Bank has two other instruments that can help countries in the area of legal and judicial reform. The first is the Institutional Development Fund (IDF), a mechanism designed to provide relatively small grants to support institution building in client countries. A significant number of IDF grants for judicial reform have been approved for transition countries:

- The Bank was asked by the government of the then Federal Republic of Yugoslavia to conduct a legal and judicial diagnostic, resulting in a \$300,000 IDF grant to support the strengthening of a court administration system.
- The Bank provided a \$296,000 grant to the American Bar Association Central and Eastern European Law Initiative's Institute in Prague to support court administrator training and development of a strategy for regional coordination and networking in ECA countries in court administration.
- Croatia received a \$350,000 grant for institutional capacity building for monitoring judicial efficiency.
- The Kyrgyz Republic has been implementing a \$350,000 grant for court information management systems.
- Romania is using a \$250,000 grant for legal drafting and regulatory management.
- Turkey has received a \$460,000 grant designed to strengthen the case-load management and court administration system and assist in the implementation of bankruptcy law amendments.
- Under an ongoing IDF for approximately \$390,000, the Slovak Republic has reorganized its court system (reducing the number of courts), initiated a reform of justice sector expenditure management, and intervened in the legal services market to make the price of legal services more affordable for the general public.

The World Bank has also undertaken a significant amount of analytic work on legal and judicial systems in transition countries. In addition to this study, other examples of recent analytic work include:

- Legal and judicial assessments of Armenia, Georgia, Moldova, Romania, Serbia and Montenegro, and the Slovak Republic.
- A 2004 regional study on institutions in southeastern Europe that includes an analysis of court enforcement and dispute resolution in the subregion.
- An analysis of problems in the judiciary in a recent public expenditure review for Romania.
- World Bank and Council of Europe collaboration to develop benchmarks for measuring the performance of judicial systems in ECA countries.¹

There continues to be a substantial demand for new work on legal and judicial reform in transition countries:

- Legal and judicial assessments are underway in FYR Macedonia and Poland, which are focused on the legal and institutional environment surrounding contract, creditor, and property rights enforcement.
- Legal and judicial policies and institutional reforms necessary to improve the investment climate will be the key focus of an upcoming adjustment loan for FYR Macedonia.
- A grant of approximately \$1 million for “Legal Aid for the Poor” is planned for Moldova. The grant will finance legal education, legal aid, and community-based consultations on legal welfare.
- In Croatia, a PAL is under preparation that aims, in part, to help improve efficiency in court proceedings, strengthen enforcement of contracts and property rights, and strengthen the role of bankruptcy trustees and administrators.
- A planned investment project in Romania will support continuing policy reforms in the judicial sector, upgrade court infrastructure (including the automation of case management), promote alternative dispute resolution, and support capacity building for a number of institutions, including the Superior Council of Magistrates, National Institute of Magistrates, and School for Clerks.

While the World Bank is still very much in the learning stage, it has gained valuable experience in how to help client governments develop

their legal and judicial institutions. The Bank has access to a variety of instruments to assist in this area, including in-depth analytic work (including both data and case study analysis), investment lending for systems reform, adjustment lending to support the design and implementation of policy reforms, and grantmaking ability through the Institutional Development Fund. We remain committed to working with clients and partner organizations in this effort.

APPENDIX 3

Methodology

This appendix provides details underlying the many charts in this report, specifically the source of the data, the specific survey questions where relevant, and other information. Please refer to box 1.1 for a summary description of each data source, as well as Web links where one can obtain more information directly from the primary source. The appendix also elaborates on endnote 13 in chapter 3 and endnote 2 in chapter 4. The descriptions can be found at the end of this appendix.

Wherever possible, this appendix gives an indication of how to interpret the statistical significance of the patterns evident on the charts. For bar charts showing changes over time, for example, this appendix describes the simple tests used to measure statistical significance. Similarly, simple tests were run for scatter plots to ensure that the apparent patterns are statistically significant. For bar charts showing patterns across countries, one should keep in mind that the ordering of countries is approximate. In general, there is no statistically significant difference between countries adjacent to each other. For example, in figure 3.6, the first figure where such an analysis is possible, the 2002 assessment by firms in Uzbekistan of the quickness of the courts is not statistically different from that of Azerbaijan or Hungary, but is statistically different from that of Armenia.

Summary Figure 1

Sources: BEEPS1, BEEPS2

Description: Respondents were asked the following question:

“How often do you associate the following descriptions with the court system in resolving business disputes? (Never, Seldom, Sometimes, Frequently, Usually, Always)

- Fair and impartial
- Honest/uncorrupted
- Quick
- Affordable
- Able to enforce its decisions.”

The chart shows the percentage of firms choosing Frequently, Usually, or Always. The data represent weighted averages of country means, with weights proportional to population.

Statistical significance was checked as described below in figure 1.1. For fairness, honesty, and affordability, all three tests showed highly significant worsening in performance. Ability to enforce decisions shows a highly significant worsening based on simple t-tests, which was not significant in controlled regressions. Quickness shows no change based on any of the three tests.

Summary Figure 2

Source: World Economic Forum, *Global Competitiveness Report 2004*

Description: See figure 3.4.

Executives participating in the Executive Opinion Survey were asked the following question: “The legal framework in your country for private businesses to settle disputes and challenge the legality of government actions and/or regulations (1 = is inefficient and subject to manipulation . . . 7 = is efficient and follows a clear, neutral process).” The chart shows the mean response for each of the country groupings. For the purposes of this chart, transition countries that are also members of the OECD (Czech Republic, Hungary, Poland, and the Slovak Republic) are included with the transition countries group. For East Asia, the values reported in the *Global Competitiveness Report* for China, Taiwan, and Hong Kong were averaged and treated as a single observation.

Summary Figure 3

Sources: BEEPS2, EBRD Transition Report, World Development Indicators

Description: See the description below for figure 3.23.

Figure I.1

Sources: BEEPS1, BEEPS2

Description: In the BEEPS2 survey, respondents were asked the following question: “Can you tell me how problematic are these different factors for the operation and growth of your business.

1=No obstacle, 2=Minor obstacle, 3=Moderate obstacle,
4=Major obstacle, 5=Don't Know

- Access to financing (for example, collateral required) or financing not available from banks
- Cost of financing (for example, interest rates and charges)
- Telecommunications
- Electricity
- Transportation
- Access to land
- Tax rates
- Tax administration
- Customs and trade regulations
- Business licensing and permits
- Labor regulations
- Skills and education of available workers
- Economic policy uncertainty
- Macroeconomic instability (inflation, exchange rate)
- Functioning of the judiciary
- Corruption
- Street crime/theft/disorder
- Organized crime/Mafia
- Anti-competitive practices of other producers
- Contract violations of by customers and suppliers
- Title or leasing of land

The indicators selected were those with perfect or very close matches between the wording on the 1999 survey and the 2002 survey. The data represent weighted averages of country means, with weights proportional to population.

Statistical significance for this and subsequent BEEPS charts was checked three ways (1) a simple t-test for difference in means, (2) pooled regressions controlling for firm characteristics, and (3) pooled regressions controlling for firm characteristics and respondent optimism.¹

In the pooled regressions controlling for firm characteristics, the right-hand side variables included the log of the firm's age, dummies for small firms, firms with foreign holdings, manufacturing firms, and city locations. The pooled regressions controlling for firm characteristics and respondent optimism include all of the same variables, plus a measure of optimism. [See Gray, Hellman, and Ryterman (2004) for details on this methodology.] In each of the pooled regression techniques, a dummy was included indicating if the observation referred to the 1999 or the 2002 data.

The differences between 1999 and 2002 in the chart are significant with a p-value of 0.001 for all three tests for labor regulations, corruption, street crime, organized crime, high taxes, policy uncertainty, and anticompetitive practices. Functioning of the judiciary and customs/foreign trade regulations were both significant for one of the three tests only—judiciary (p-value of 0.040) for the characteristics and optimism regression, and customs/foreign trade regulations (p-value of 0.062) for the simple t-tests. Business licensing showed a significant worsening for all three tests (p-values: 0.053 for t-tests, 0.011 for characteristics, and 0.004 for characteristics plus optimism).

Figure 2.1

Source: World Values Survey²

Description: Sample sizes ranged from 1,173 in Slovenia to 1,488 in the Slovak Republic. (In the WVS database, data are reported separately for jurisdictions within a single country, for example, in the Czech Republic and the Slovak Republic.) The data refer to the 1990 round of the survey.

Respondents were asked the following question: “There is a lot of discussion about how business and industry should be managed. Which of these four statements comes closest to your opinion?”

1. The owners should run their business or appoint the managers.
2. The owners and the employees should participate in the selection of managers.

3. The government should be the owner and appoint the managers.
4. The employees should own the business and should elect the managers.”

The chart reflects the percentage of respondents that selected 3 of those who selected any of 1-4.

Figure 2.2

Source: EBRD Legal Indicator Survey, 1999³

Description: The *EBRD Legal Indicator Survey* was conducted annually from 1998–2002. The survey was sent to reputable law firms in each country. Samples were very small—ranging from 21 in Russia to 1 in Belarus—so the responses for some countries are more akin to expert assessments than survey averages. Despite the small samples, simple t-tests for differences of means indicate statistical differences between many country pairs. Only Albania, Belarus, Georgia, and Kazakhstan are not statistically different from any other country at the 10 percent level.

Respondents were asked the following question: “Are draft laws affecting investment published and accessible to practitioners?”

- 1 = Never
- 2 = Rarely
- 3 = Sometimes
- 4 = Frequently
- 5 = Almost Always.”

The chart reflects the mean of the responses.

Figure 2.3

Source: EBRD Legal Indicator Survey, 1999

Description: The *EBRD Legal Indicator Survey* is described above for figure 2.2.

Respondents were asked the following question: “Are draft laws affecting investment published and accessible to practitioners?”

If yes, is there an opportunity for parties to comment on draft laws?

- 1 = Never
- 2 = Rarely

3 = Sometimes
 4 = Frequently
 5 = Almost Always.”

The chart reflects the mean of the responses.

Figure 2.4

Sources: Centre for the Study of Public Policy, “New Democracies Barometer” and “New Russia Barometer”⁴

Description: The data come from stratified nationwide samples representing all adults over the age of 18 with at least 1,000 respondents per country.

Respondents in Russia were asked the following question: “To what extent do you trust different institutions in our society? Please show me on this 7-point scale.” The list of institutions included, among others, the courts and Duma (Parliament). Respondents in all other countries were asked the following question: “There are many different institutions in this country, for example, government, the courts, police, civil servants. Please show me on this 7-point scale, where 1 represents no trust and 7 great trust, how great your personal trust is in each of these institutions.” The list of institutions included, among others, courts, parliament, and government. The chart reflects the percentage of respondents giving a positive rating, 5 to 7.

Figure 2.5

Sources: Centre for the Study of Public Policy, “New Democracies Barometer” and “New Russia Barometer”

Description: See the description above for figure 2.4. The chart reflects the ratio of the level of trust in courts to the average level of trust in parliament and government. Thus a value of 1 would indicate equal levels of trust. For Russia, the government was not included in the survey so the bar reflects the ratio of trust in courts to parliament.

Figure 3.1

Source: EBRD Legal Indicator Survey, 1999

Description: See the description above for figure 2.2. Both indicators are based on the *EBRD Legal Indicator Survey*'s commercial law questions (covering secured transaction, company law, and bankruptcy). Legal extensiveness represents the degree to which a formal legal framework of commercial laws exists and includes questions such as: "Does the document creating the security interests have to be notarized to be enforceable against third parties?" Legal effectiveness represents the degree to which those laws are implemented in practice and includes questions such as: "Have companies complied with court decisions after being sued by shareholders?"

Figure 3.2

Source: EBRD Legal Indicator Survey, 1999 and 2002

Description: The chart depicts the changes in the extensiveness and effectiveness indicators as described above for figure 3.1.

Figure 3.3

Source: ABA–CEELI Judicial Reform Index

Description: The ABA–CEELI JRI is generated by expert assessments for each of 14 countries: Albania, Armenia, Bosnia and Herzegovina, Bulgaria, Croatia, FYR Macedonia, Kazakhstan, Kyrgyz Republic, Moldova, Romania, Serbia and Montenegro, Slovak Republic, Ukraine, and Uzbekistan. The JRI rates each of the 30 dimensions shown as positive, neutral, or negative. These have been assigned values of +100, 0, or –100. An average score of 0, therefore, means that the number of countries with ratings of positive exactly equals the number of countries with ratings of negative.

The dimensions shown in this figure are defined as follows:

- **Judicial Immunity for Official Actions.** Judges have immunity for actions taken in their official capacity.
- **Guaranteed Tenure.** Senior level judges are appointed for fixed terms that provide a guaranteed tenure, which is protected until retirement age or the expiration of a defined term of substantial duration.
- **System of Appellate Review.** Judicial decisions may be reversed only through the judicial appellate process.

- **Judicial Associations.** An association exists, the sole aim of which is to protect and promote the interests of the judiciary, and this organization is active.
- **Public and Media Access to Proceedings.** Courtroom proceedings are open to, and can accommodate, the public and the media.
- **Judicial Jurisdiction over Civil Liberties.** The judiciary has exclusive ultimate jurisdiction over all cases concerning civil rights and liberties.
- **Judicial Review of Legislation.** A judicial organ has the power to determine the ultimate constitutionality of legislation and official acts, and such decisions are enforced.
- **Judicial Oversight of Administrative Practice.** The judiciary has the power to review administrative acts and to compel the government to act where a legal duty to act exists.
- **Judicial Conduct Complaint Process.** A meaningful process exists under which other judges, lawyers, and the public may register complaints concerning judicial conduct.
- **Minority and Gender Representation.** Ethnic and religious minorities, as well as both genders, are represented in the pool of nominees and in the judiciary generally.
- **Removal and Discipline of Judges.** Judges may be removed from office or otherwise punished only for specified official misconduct and through a transparent process, governed by objective criteria.
- **Selection/Appointment Process.** Judges are appointed based on objective criteria, such as passage of an exam, performance in law school, other training, experience, professionalism, and reputation in the legal community. While political elements may be involved, the overall system should foster the selection of independent, impartial judges.
- **Judicial Positions.** A system exists so that new judicial positions are created as needed.
- **Judicial Qualification and Preparation.** Judges have formal university-level legal training and have practiced before tribunals or, before taking the bench, are required (without cost to the judges) to take relevant courses concerning basic substantive and procedural areas of the law, the role of the judge in society, and cultural sensitivity.
- **Objective Judicial Advancement Criteria.** Judges are advanced through the judicial system on the basis of objective criteria such as ability, integrity, and experience.

- **Case Filing and Tracking Systems.** The judicial system maintains a case filing and tracking system that ensures cases are heard in a reasonably efficient manner.
- **Court Support Staff.** Each judge has the basic human resource support necessary to do his or her job, for example, adequate support staff to handle documentation and legal research.
- **Continuing Legal Education.** Judges must undergo, on a regular basis and without cost to them, professionally prepared continuing legal education courses, the subject matters of which are generally determined by the judges themselves and which inform them of changes and developments in the law.
- **Code of Ethics.** A judicial code of ethics exists to address major issues such as conflicts of interest, ex parte communications, and inappropriate political activity, and judges are required to receive training concerning this code both before taking office and during their tenure.
- **Adequacy of Judicial Salaries.** Judicial salaries are generally sufficient to attract and retain qualified judges, enabling them to support their families and live in a reasonably secure environment, without having to have recourse to other sources of income.
- **Contempt/Subpoena/ Enforcement.** Judges have adequate subpoena, contempt, and/or enforcement powers, which are used, and these powers are respected and supported by other branches of government.
- **Case Assignment.** Judges are assigned to cases by an objective method, such as by lottery, or according to their specific areas of expertise, and they may be removed only for good cause, such as a conflict of interest or an unduly heavy workload.
- **Judicial Security.** Sufficient resources are allocated to protect judges from threats such as harassment, assault, and assassination.
- **Judicial Buildings.** Judicial buildings are conveniently located and easy to find, and they provide a respectable environment for the dispensation of justice with adequate infrastructure.
- **Distribution and Indexing of Current Law.** A system exists whereby all judges receive current domestic laws and jurisprudence in a timely manner, and there is a nationally recognized system for identifying and organizing changes in the law.
- **Budgetary Input.** The judiciary has a meaningful opportunity to influence the amount of money allocated to it by the legislative and/or executive branches, and, once funds are allocated to the judiciary, the

judiciary has control over its own budget and how such funds are expended.

- **Judicial Decisions and Improper Influence.** Judicial decisions are based solely on the facts and law without any undue influence from senior judges (for example, court presidents), private interests, or other branches of government.
- **Computers and Office Equipment.** The judicial system operates with a sufficient number of computers and other equipment to enable it to handle its caseload in a reasonably efficient manner.
- **Publication of Judicial Decisions.** Judicial decisions are generally a matter of public record, and significant appellate opinions are published and open to academic and public scrutiny.
- **Maintenance of Trial Records.** A transcript or some other reliable record of courtroom proceedings is maintained and is available to the public.

Figure 3.4

Source: World Economic Forum, *Global Competitiveness Report 2004*⁵

Description: For each of the years shown in the chart, the *Executive Opinion Survey*, published in the *Global Competitiveness Report*, asks respondents questions about the ability of private parties to use legal channels to challenge the state. Unfortunately, the wording of the question changed somewhat from year to year, making it impossible to compare country scores in an absolute sense. However, since the questions were all broadly similar, an alternative approach is to examine how each country's responses compared to other countries, year by year. The chart shows the number of standard deviations from the mean across all EU and transition countries. For the purposes of this chart, the new EU members are displayed separately.

The 14 EU states covered by the survey were Austria, Belgium, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Netherlands, Portugal, Spain, Sweden, and the United Kingdom.

The following questions were asked:

- **1998 Q:** Private businesses can readily file lawsuits at independent and impartial courts if there is a breach of trust on the part of government. (1 = strongly disagree, 7 = strongly agree)
- **1999 Q:** Private business has recourse to independent and impartial courts for challenging the legality of government actions and/or regulations. (1 = strongly disagree, 7 = strongly agree)

- **2000 Q:** A legal framework exists for private businesses to challenge the legality of government actions and/or regulations. (1 = strongly disagree, 7 = strongly agree)
- **2001 Q:** A trusted legal framework exists for private businesses to challenge the legality of government actions and/or regulations. (1 = strongly disagree, 7 = strongly agree)
- **2002/3 Q:** The legal framework in your country for private businesses to settle their disputes and challenge the legality of government actions and/or regulations. (1 = is inefficient and subject to manipulation, 7 is efficient and follows a clear, neutral process)
- **2003/4 Q:** The legal framework in your country for private businesses to settle disputes and challenge the legality of government actions and/or regulations. (1 = is inefficient and subject to manipulation, 7 = is efficient and follows a clear, neutral process)

The mean responses to these questions are published in the *Global Competitiveness Reports*. For each country-year, the number of standard deviations from the mean of the 14 EU countries and the 6 transition countries was calculated. To make the chart manageable, only the 1998, 2001, and 2003/4 responses are reported.

Figure 3.5

Source: ABA–CEELI Judicial Reform Index

Description: See description above for figure 3.3. Efficiency is an index composed of the following five components: court support staff, judicial positions, case filing and tracking systems, computers and office equipment, and distribution and indexing of current law. Independence is an index composed of the following eight components: selection/appointment process, judicial oversight of administrative practice, system of appellate review, contempt/subpoena/enforcement, budgetary input, guaranteed tenure, judicial immunity for official actions, and judicial decisions and improper influence.

Figure 3.6

Sources: BEEPS1, BEEPS2

Description: Respondents were asked the following question: “How often do you associate the following descriptions with the court system

in resolving business disputes? (Never, Seldom, Sometimes, Frequently, Usually, Always)

- Fair and impartial
- Honest/uncorrupted
- Quick
- Affordable
- Able to enforce its decisions.”

The chart shows the percentage of firms choosing Frequently, Usually, or Always.

Statistical significance was checked as described in figure 1.1. The threshold for statistical significance is 10 percent. In the vast majority of cases, the regressions confirmed the results of the simple t-tests, so the t-tests are used as the basis for the note in the chart about statistical significance.

Figures 3.7 and 3.8

Source: Doing Business database (2004)⁶

Description: The charts show the total and average length of time for collecting on a debt, reported by the three phases indicated. The data for 2004 are taken from *Doing Business in 2005*.

Figure 3.9

Sources: BEEPS1, BEEPS2

Description: See the description above for figure 3.6. The threshold for statistical significance is 10 percent. In the vast majority of cases, the regressions confirmed the results of the simple t-tests, so the t-tests are used as the basis for the note in the chart about statistical significance.

Figure 3.10

Source: ABA–CEELI Judicial Reform Index

Description: See description above for figure 3.3. Independence is an index composed of the following eight components: selection/appointment process, judicial oversight of administrative practice, system of appellate review, contempt/subpoena/enforcement, budgetary input, guaranteed

tenure, judicial immunity for official actions, and judicial decisions and improper influence. Accountability and Transparency is an index composed of the following five components: code of ethics, judicial conduct complaint process, public and media access to proceedings, publication of judicial decisions, and maintenance of trial records.

Simple regressions were run to ensure that the relationships were statistically significant. The p-value for an OLS regression is 0.087, and the p-value for “robust” regression, using iteratively reweighed least squares to address the possibility of strong outliers, is 0.023.

Figure 3.11

Sources: BEEPS1, BEEPS2

Description: See the description above for figure 3.6. The threshold for statistical significance is 10 percent. In the vast majority of cases, the regressions confirmed the results of the simple t-tests, so the t-tests are used as the basis for the note in the chart about statistical significance. This variable provided the exception to the rule, however. Both Hungary and Estonia exhibit statistically significant improvements based on t-tests (5 percent level), but both exhibit statistically significant deterioration based on the regressions (5 percent and 10 percent levels).

Figure 3.12

Sources: BEEPS1, BEEPS2

Description: See the description above for figure 3.6. The threshold for statistical significance is 10 percent. In the vast majority of cases, the regressions confirmed the results of the simple t-tests, so the t-tests are used as the basis for the note in the chart about statistical significance.

Figure 3.13

Sources: BEEPS1, BEEPS2

Description: Respondents were asked: “Thinking now of unofficial payments/gifts that a firm like yours would make in a given year, could you please tell me how often would they make payments/gifts for the following purposes . . . To deal with courts (Never, Seldom, Sometimes,

Frequently, Usually, Always)” . . . The chart shows the mean response. The threshold for statistical significance is 10 percent. In the vast majority of cases, the regressions confirmed the results of the simple t-tests, so the t-tests are used as the basis for the note in the chart about statistical significance.

Figure 3.14

Sources: EBRD Legal Indicator Survey, BEEPS2

Description: The *EBRD Legal Indicator Survey* is described above for figure 2.2. Respondents were asked the following questions:

“How does the average annual salary of a judge of a court of first instance compare with that of (1) a private lawyer, and (2) an entry level primary school teacher? Using an index of 100 for such a judge, please complete

Judge of court of first instance. 100
 Private lawyer _____
 Entry-level primary school teacher _____”

The ratios of salaries of judges to private lawyers were constructed from these responses. The assessment of the fairness of courts is described in the notes above for figure 3.6.

As noted above, the number of observations available for the EBRD LIS varied. This was addressed in two ways: First, countries with only a single observation for this variable (Bosnia and Herzegovina, the Kyrgyz Republic, and Tajikistan) were dropped. Second, a weighted regression, with weights proportional to the number of observations on which the mean was computed, was added to the OLS and robust regressions for examining statistical significance. The p-value for an OLS regression is 0.068; the p-value for “robust” regression, using iteratively reweighted least squares to address the possibility of strong outliers, is 0.026; and the p-value for weighted least squares is 0.013.

Figure 3.15

Sources: BEEPS1, BEEPS2

Description: See the description above for figure 3.6. The threshold for statistical significance is 10 percent. In the vast majority of cases, the regressions confirmed the results of the simple t-tests, so the t-tests are used as the basis for the note in the chart about statistical significance.

Figure 3.16

Sources: BEEPS2 and Doing Business (2003)

Description: Respondents to the BEEPS were asked the following question:

“Can you tell me how problematic are these different factors for the operation and growth of your business?”

Contract violations of by customers and suppliers

1=No obstacle

2=Minor obstacle

3=Moderate obstacle

4=Major obstacle

5=Don't Know”

The mean response (after dropping responses of “don't know”) is on the vertical axis.

The *Doing Business* database includes a summary index of procedural complexity for enforcing a contract, and this is depicted on the horizontal axis. The chart uses 2003 data to more closely correspond with the 2002 data on the vertical axis.

Figure 3.17

Sources: BEEPS2, EBRD Transition Report, 2002

Description: The EBRD Transition Reports include nine indicators covering various aspects of the reform process in transition countries. The variable on the horizontal axis is the simple average of these nine indicators: large-scale privatization, small-scale privatization, governance and enterprise restructuring, price liberalization, trade and foreign exchange system, competition policy, banking reform and interest rate liberalization, securities market and nonbank financial institutions, and infrastructure.

In the BEEPS2 survey, respondents were asked the following question: “How many cases in civil or commercial arbitration courts have

involved your enterprise either as a plaintiff or defendant since January 2000?” The number on the vertical axis represents the percentage of respondents that had been to court at least once.

The p-value for an OLS regression is 0.073; the p-value for “robust” regression, using iteratively reweighed least squares to address the possibility of strong outliers, is 0.105.

Figure 3.18

Source: BEEPS2

Description: In the BEEPS2 survey, respondents were asked the following questions: “How many cases in civil or commercial arbitration courts have involved your enterprise either as a plaintiff or defendant since January 2000?” The number on the horizontal axis represents the percentage of respondents that had been to court at least once. The number on the vertical axis represents the percentage of respondents that described the courts as “quick.” See description for figure 3.6, above, for a full description of the survey question.

The p-value for an OLS regression is 0.001; the p-value for “robust” regression, using iteratively reweighed least squares to address the possibility of strong outliers, is 0.001.

Figure 3.19

Source: BEEPS2

Description: The number on the horizontal axis represents the percentage of respondents that had been to court at least once. See above for a full description of the survey question. The number on the vertical axis represents the percentage of respondents that described the functioning of the judiciary as a moderate or major problem doing business (after dropping responses of “don’t know”). See the notes for figure 1.1 for a full description.

The p-value for an OLS regression is 0.002; the p-value for “robust” regression, using iteratively reweighed least squares to address the possibility of strong outliers, is 0.001.

Figure 3.20

Sources: BEEPS1, BEEPS2

Description: See notes for figure 1.1 for a description of the question in the BEEPS2 survey. In 1999, the categories were identical and the question was worded as follows: “Using this scale can you tell me how problematic these different factors are for the operation and growth of your business.” One of the assessed categories was “functioning of the judiciary.”

The threshold for statistical significance is 10 percent. In the vast majority of cases, the regressions confirmed the results of the simple t-tests, so the t-tests are used as the basis for the note in the chart about statistical significance.

Figure 3.21

Source: BEEPS2

Description: See notes for figure 1.1 for a description of the question in the BEEPS2 survey. The second bar represents an index of all other problems firms were asked to evaluate. In some cases, the “other problems” did not match exactly, so indices of the closest possible comparison were made.

The threshold for statistical significance is 10 percent; however for this chart, nearly all of the differences were significant at the 1 percent level. The regression techniques used for assessing changes over time could not be used in this case, since both bars are based on 2002 data and the sample characteristics did not vary across the bars.

Figure 3.22

Sources: BEEPS1, BEEPS2

Description: As described in the text, for each year an indicator of the judiciary as a problem doing business (described above in figure 3.19) was regressed on indicators of fairness and honesty, quickness, affordability, and ability to enforce decisions (described above for figures 3.6, 3.9, 3.11, 3.12, and 3.15). The regression coefficients are plotted.

All of the coefficients in the individual country regressions were significantly different from zero except for affordability in 2002. In order to

test whether the coefficients are different between the years, the data were pooled for both years and the regression allows each factor-year to have different slopes, as well as fixed effects for each country-year. The coefficient estimates correspond exactly to the ones presented in figure 3.22, based on separate regressions for 1999 and 2002, but allow to test directly whether the differences between 1999 and 2002 are significant. The differences between 1999 and 2002 are significant for speed (1 percent level) and affordability (5 percent level), but not for fairness/honesty or ability to enforce decisions.

Figure 3.23

Sources: BEEPS2, EBRD Transition Report, World Development Indicators

Description: The horizontal axis shows the log of GDP per capita in 2002. The vertical axis shows a simple average of the percentage of firms that have been to court (see notes for figure 3.18) and the average EBRD transition indicator (see notes for figure 3.17).

Figure 3.24

Sources: BEEPS2, EBRD Transition Report, World Development Indicators.

Description: The axes are as described above for figure 3.23. The bars show the average assessment of the judiciary as a problem doing business (as described in the notes for figure 3.20) across countries in that cell.

Figure A1.1

Source: Executive Opinion Survey

Description: The EOS is described above for figure 3.4. Respondents were asked to assign a score in response to the following statement: “The judiciary in your country is independent from political influences of members of government, citizens, or firms (1 = no, heavily influenced, 7 = yes, entirely independent).” The chart shows the mean response. The countries included are those for which data were available: CIS (Russia and Ukraine), EU8 (Czech Republic, Estonia, Hungary, Latvia, Lithuania,

Poland, the Slovak Republic, and Slovenia), SEE (Bulgaria, Croatia, Macedonia, FYR, Romania, and SAM), and Turkey.

Figure A1.2

Source: BEEPS2

Description: See description of the question for figure 3.6. The country groupings are: CIS (Armenia, Azerbaijan, Belarus, Georgia, Kazakhstan, the Kyrgyz Republic, Moldova, Russia, Tajikistan, Ukraine, and Uzbekistan), EU8 (Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, the Slovak Republic, and Slovenia), SEE (Albania, BiH, Bulgaria, Croatia, Macedonia, FYR, Romania, and SAM), and Turkey.

Figures A1.3 and A1.4

Source: Doing Business (2003)

Description: The *Doing Business* database is described above for figures 3.7 and 3.8. The cost and time to enforce a contract are among the measures used in the *Doing Business* database. The country groupings are as described above for figure A1.2, except that data were not available for Estonia and Tajikistan.

Figure A1.5

Source: BEEPS2

Description: See description of the question for figure 3.15. The country groupings are as described above for figure A1.2.

Figure A1.6

Source: BEEPS2

Description: Respondents to the BEEPS survey were asked “To what degree do you agree with this statement? ‘I am confident that the legal system will uphold my contract and property rights in business disputes.’ 1=Never, 2=Seldom, 3=Sometimes, 4=Frequently, 5=Usually, 6=Always.” The chart shows the percentage of firms answering 4, 5, or 6. The country groupings are as described above for figure A1.2.

Chapter 3, Endnote 13

As alluded to in the footnote, the complex relationship between firm perceptions of the qualities of the courts, their use of courts, and the influence of market reforms was examined in a three equation model: (1) firms' use of courts depends on their assessment of how problematic courts are and their transactional demand for courts, measured by the average EBRD transition indicator and the firm's indication of how problematic contract violations are for the firm; (2) firms assess how problematic courts are based on the overall pressure on courts and by assessments of the qualities of courts (quick, fair and honest, etc.); (3) the speed of courts depends on pressure by the number of users and by the overall capacity of the country to support the courts, proxied by GDP per capita. The system was estimated by three-stage least squares and the detailed results are presented in table A3.1. This methodology draws on Peter Murrell (2001).

The results of the estimation generally support the bivariate relationships described in the text. Countries where firms are perceived in a more positive light, for example as "quick," tend to have better (that is, lower) perceptions of the courts as a problem for doing business. Countries that have more pressure on courts, for example with high values of "contract violations as a problem" and that have progressed farther on the transition path as measured by the average EBRD indicator, tend to have more firms availing themselves of the courts. Finally, countries where firms make more use of courts also tend to have slower courts, as measured by firms' perceptions of court speed.

Certain aspects of this relationship are extremely robust to alternative specifications, notably the relationship between use of courts and assessments of speed (line 1), the influence of contract violations (3), and the impact of transition progress (5). Much less stable is the impact of the "judiciary as a problem" variable on the use of courts (4), which has a significant positive sign in some specifications.

Chapter 4, Endnote 2

The analysis included regressions of courts as a problem on each of the four aspects of courts plus firm-level characteristics (for firms that have been to court only). For each country that had sufficient observations, the p-value was recorded for the test of the joint restriction that all of the four

Table A3.1 Estimation of the relationship between court use, court speed, and perceptions of the qualities of courts

| Variable | Coefficient |
|--|--------------------|
| <i>Endogenous variables in bold</i> | <i>(p-value)</i> |
| Average assessment of whether courts are “quick” = | |
| (1) Percentage of firms using courts | −4.12*** (0.00) |
| (2) GDP per capita | 1.35 (0.18) |
| Percentage of firms using courts = | |
| (3) Average assessment of “contract violations” as a problem | 2.08** (0.04) |
| (4) Average assessment of “functioning of the judiciary” as a problem | 0.32 (0.75) |
| (5) Average EBRD Transition Indicator | 2.38** (0.02) |
| Average assessment of “functioning of the judiciary” as a problem = | |
| (6) Percentage of firms using courts | −1.81* (0.07) |
| (7) Average assessment of whether courts are “quick” | −3.26*** (0.00) |
| (8) Average assessment of whether courts are “fair and honest” | −0.60 (0.55) |
| (9) Average assessment of whether courts are “affordable” | −1.59 (0.11) |
| (10) Average assessment of whether courts are “able to enforce decisions” | −0.33 (0.74) |

Sources: BEEPS2; World Development Indicators; EBRD Transition Report.

Note: Significance levels: ***=1%, **=5%, *=10%. Estimated by three-stage least squares. P-values are in parentheses. All data are for 2002. All equations included constants, not reported here. Assessments of courts and their qualities based on perceptions of court users only.

aspects of the courts are equal to zero. This p-value is an inverse indicator of how well the assessment of problems is explained by variation in the assessments of the courts. Regressing the distance from the origin on the p-value yields a coefficient that is significant at the 5 percent level. After dropping countries with less than 30 degrees of freedom (41 observations), the significance level falls to less than 1 percent. An interpretation of this pattern is that when firms in countries near the origin in the

typology say courts are problematic, they seem to be reporting a general malaise or distrust, rather than reflecting any of the four specific aspects we examined. Firms in countries further from the origin, in contrast, tend to be reporting on specific aspects of the experience. The CEE countries, for example, are most likely to have something stand out as best explaining what firms mean when they say courts are problematic.

A useful analogy illustrating the relevance for policy is provided by a standard production possibilities frontier. If far inside the frontier, then there is not really an issue of trade-offs—the goal is just to try to get closer to the frontier. At the other extreme, on the production possibilities frontier there are always trade-offs. The analogy for the typology in figure 3.23 is straightforward. In countries with little demand for or capacity for judicial services, little can be gained by a sophisticated and nuanced reform strategy—the first goal is to make the court relevant. Among the EU members of the upper right-hand cell, in contrast, there are gains from understanding the specific weaknesses of the courts.

Notes

Appendix 1

1. The information in this appendix draws from the following sources: Cakmak 2002; European Commission 1999, 2000, 2003; Inalcik (trans.) and Hurewitz (ed.) 1975; Özücü, 1992, 1999; and Turkish Industrialists' and Businessmen's Association 1999.
2. Turkey was the subject of a significant number of judgments of the European Court for Human Rights on the provision of "fair trials" (other than the length of court proceedings) in 2003. See the Caseload of the European Court of Human Rights available at: <http://echr.coe.int/Eng/Judgments.htm>.

Appendix 2

1. The first report based on this evaluation exercise with data for 2002 was adopted by the Council of Europe's European Commission for the Efficiency of Justice in December 2004, and will be repeated bi-annually. See <http://www.coe.int/cepej>.

Appendix 3

1. Respondent optimism was identified as an important factor for understanding firm responses related to corruption in Gray, Hellman, and Ryterman (2004).
2. World Values Study Group, 1981–4 and 1990–3; 2nd ICPSR version 1999; and Inter-university Consortium for Political and Social Research, 1999.
3. Ramasastry 2002.
4. Rose 2002; Rose and Haerpfer 1994, 1996, 1998.
5. World Economic Forum 1998, 1999, 2000, 2001, 2002/3.
6. World Bank 2004.

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