

Taking Legal Origins Theory Seriously

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John Armour et al., *Law and Financial Development: What We Are Learning from Time-series Evidence* (2010), at [SSRN](#).

In the late 1990s, Rafael La Porta, Florencio Lopez-de-Silanes, Andrei Shleifer, and Robert W. Vishny (“LLSV”) launched a research project examining connections between legal rules governing investor protection and economic development. Working on the assumption that legal rules could be measured and quantified, LLSV purported to demonstrate that common law countries were more protective of outside investors – and, thus, more hospitable to economic development – than civil law countries. In the ensuing years, LLSV and other economists have expanded and refined their work, constructing the grandly named Legal Origins Theory, which holds that legal systems are important determinants of economic development. The influence of Legal Origins Theory is not confined to economics journals, but may be seen in policy reforms through the [World Bank’s Doing Business reports](#).

While many legal scholars have dismissed this work because of its naïve assumptions about law and legal change, especially in early papers, a group of legal scholars at Cambridge University – led by Simon Deakin, John Armour, and Ajit Singh – took Legal Origins Theory seriously. Embracing the assumption that legal rules could be measured and quantified (“leximetrics”), the Cambridge Group produced legally sophisticated datasets on shareholder protection, creditor protection, and labor regulation. In [Law and Financial Development: What We Are Learning from Time-series Evidence](#), published as part of a recent symposium on Legal Origins Theory in the [BYU Law Review](#), four members of the Cambridge Group take stock of what we have learned from those datasets and chart some new directions for future research.

Critics of Legal Origins Theory will not be surprised to learn that the Cambridge Group finds little support for the theory in longitudinal data. While shareholder protections and corporate governance standards have been strengthened worldwide – reflecting the efforts of civil law countries to catch up with common law countries – these legal changes have not resulted in more dispersed share ownership and increased stock market activity, as predicted by Legal Origins Theory. According to Armour et al., these considerable legal reforms suggest that “lock-in through legal origin has not been much of an obstacle to the formal convergence of systems.” More importantly, legal reforms have not led to greater economic development. The authors offer alternative interpretations of their results:

One possible interpretation of our results is that a “one size fits all” approach to corporate governance reforms, stressing elements of British and American practice—the role of independent boards and the market for corporate control—may not be working as intended in civilian and developing systems. Another interpretation is that even in the common law world, shareholder protection can have counterproductive effects, by unnecessarily raising the costs associated with a stock exchange listing.

For those who remain interested in attempts to discern connections between law reform and economic development along the lines suggested by Legal Origins Theory, Armour et al. urge a reconceptualization of the role of legal systems: “legal systems are not the independent, ‘exogenous’ force that legal origins theory takes them to be. Legal systems are, to some degree, ‘endogenous’ in the sense of being shaped by their economic and political environment.”

The work of the Cambridge Group is an important part of the most significant research advance on corporate governance since the advent of law and economics in the 1970s and 1980s. The analysis by the Cambridge Group has called into question many of the central tenets of Legal Origins Theory, but in my view, the more important long-term contributions of this work are twofold: (1) the work has gone a long ways toward legitimating “leximetrics” in studies of comparative corporate governance, and (2) the work has reignited interest in comparative corporate governance, a field that has traditionally suffered from a perceived lack of rigor.

This may seem a bit hyperbolic, but I believe that this work has paved the way for a re-examination of the whole of corporate law from an empirical, comparative perspective. Such work requires more resources than the traditional corporate law scholarship, but the Cambridge Group has demonstrated the power of leximetrics to provide new insights. One can imagine using these techniques to compare various states in the U.S. or various countries in Europe along any dimension of law that might possibly be related to economic development.

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