All Quiet on the Eastern Front

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Introduction

The title that I have chosen for this essay is something of a contradiction in terms. There have been enormous upheavals in Eastern Europe during the past two years. Indeed, it is unlikely that the pace of innovation and surprise will slacken in the future, even if its direction may change in unexpected, and even unwelcome, ways. There will be many testimonies to the enormous shifts that have taken place there, to the fond hopes that have been realized, as in Hungary and perhaps Poland or Czechoslovakia, and to those that have been dashed, as in Romania. If each day's events brings us news of ferment and change, then why now of all times would anyone have the temerity to make an ironic play on words on Erich Maria Remarque's classic of another era, *All Quiet on the Western Front*?

There are reasons for this apparent twist, stemming from the two ways to look at the transformative events in Eastern Europe. One way speaks of culture and transition and thrives upon local knowledge. The other looks at the ebb and flow of events from the loftier reaches of political and constitutional theory. Each is worth a bit of elaboration.

The first approach concentrates on the shift from monolithic political control to (if we are lucky when the dust settles) some form of democratic government—a form of government that constantly probes the uncertain line between market and government ordering. Making an accurate assessment of the way events will play out requires an enormous amount of knowledge about specific conditions that is clearly beyond the ken of the outsider, and in all likelihood the insider as well. There are always questions of transition that are by nature heavily fact-specific. As the standard analysis of game theory (or at least chaos theory) so well shows, the ultimate outcome in a complete game is often highly sensitive to small

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changes in initial position, the importance of which is apt to elude both participant and observer alike.[1] There is therefore a sense in which each day's news will bring anticipation and disappointment, so that the academic analysts come to resemble (and the image is chosen deliberately) Wall Street pundits who can speak with total confidence about the reason why the market performed as it did today, but are utterly at sea in trying to explain how it will respond tomorrow.[2] (I will say only that the first draft of this essay was written six months ago, and its cautious conclusions have not been falsified in my view by interim events.)

But what about the second approach? My only possible claim to knowledge has less to do with the prediction of events and more to do with the broad-gauged normative and positive analysis of the situation. These normative and positive approaches are conceptually distinct, but they tend to blend imperceptibly in practice and I shall not work overtime to keep them separate. The question in its starkest form is one of political knowledge: What can we learn from Eastern Europe and its recent history, and what can the Eastern Europeans learn from us and our somewhat longer and more successful historical romance with that uneasy cross between popular democracy and constitutional government?

One ungracious response to these questions is that we can learn nothing at all. That conclusion resonates with those who believe that history is a disconnected set of "contingent" events that resists the application of general or covering laws. After all, if history is only a collection of episodes that follow loosely one after the other, why should we think that our history will tell us much about the very different tradition and culture of Eastern Europe? Indeed, we could go one step further and ask why we should expect that the Poles should learn from the Hungarians, or the Bulgarians from either: if the only thing that these various nations share is a common rejection of their communist past, there is little that should bind them together for a common democratic future. To the skeptic, the want of historical laws and the uniqueness of historical events defeats any effort at generalization, either of understanding or prediction.

This last argument has both strong and weak points. It seems clear to me that there is little that we can learn from Eastern Europe. So in one sense I accept the skeptic's position. But my reason is the exact opposite of the one the skeptic commonly advances.

[1] See, for example, James Gleick, *Chaos: Making a New Science* ch 1 (Viking, 1987).

[2] See Burton Gordon Malkiel, *A Random Walk Down Wall Street* (Norton, 1990).

The reason that we can learn little from the events in Eastern Europe is that the basic principles that will determine the success or failure of a system of governance are already well known to those who pay attention to the lessons of theory and history. The most that Eastern Europe can tell us is that the past shows the permanent and irremediable defects of a system of centralized control of the productive activities of a given society, whether political or economic. The future will tell us whether the peoples of Eastern Europe have learned that lesson or whether, because of the problems of collective deliberation in times of crisis, each in its own way will fritter away an opportunity that comes but infrequently to any nation. The reason we can learn very little about first principles from the Eastern European nations is not because their contingent circumstances are so far removed from our own. Quite the opposite: the reason we can learn so little from them is that the general theory of sound governance travels well abroad. If we understand how the system works (or should be made to work) at home, then we should understand whether it will flourish or fail in other settings.

A short defense of my position seems appropriate. I will explore the proposition of universal first principles in the contexts of common law adjudication and constitution-making. The development of these themes takes place at several stages, all of which stress how a few core principles are sufficient to organize our understanding of both private and public law. Section I therefore gives a brief account of the central and universal principles of private law—principles as applicable to business relations in Eastern Europe as anywhere else in the world. Section II then recapitulates in brief form the basic principles of constitutionalism, which again are as applicable to Eastern Europe as to the democracies of Western Europe and the United States: separation of powers, federalism, and protection of individual rights (including economic liberties). Section III then explores the failure of gradualism, and notes that there are as many hidden perils in the politics of prudence as there are in the politics of radical change. Eastern Europe faces three problems: the first is that of transition; the second is the pressing need to deal with the questions of racial and ethnic divisions; and the third is its inability to forge a durable social consensus on the necessity of strong institutions of private property for both political liberty and economic growth. Taken together, these three points lead to a pessimistic conclusion. It will take uncommon foresight, heroic measures and massive good fortune for Eastern Europe to hit upon the constitutional measures and economic

policies needed to overcome the devastation wrought by communist political rule and socialist economic order.

I. First Principles and the Common Law

A. Common Law Rules

About ten years ago, I attacked the popular proposition that the rules of sound common law should change with time and circumstance.[3] Under the standard view, the great judges are the innovators. They recognize legal obsolescence when they see it, and then move courageously past old precedents in order to create a body of common law rules that is more in harmony with the current times. Those judges who simply reiterate the ostensible wisdom of the past, who naively believe that law is found and not made, are condemned to a second-class status within the legal firmament: good technicians without bold legal imagination.

In my view, this common perception seriously misconceives the role of a great judge. To be sure, it may take some legal imagination to apply the old rules to a novel set of circumstances. But in this context, the genius of the judge lies not in the way he repudiates the common law rules of the past but rather how he extends them to situations that do not fall precisely within their ambit.

For example, a judge with a powerful grasp of the rules of trespass to land and chattels should be able to proceed by analogy to provide protection to various forms of intangible property, noting both the similarities and differences between the new and old situations. Thus, if there are strong rules that protect land against trespass, and somewhat weaker rules (for example, live and let live) that protect land against nuisance, the able judge is one who can decide whether the trespass or the nuisance paradigm should apply to the new situation in which the same portion of the spectrum is covered by rival radio or television broadcasters, and resisted by ordinary landowners. The judge should be able to determine that the principle of reciprocal nuisances rests on the proposition that all landowners are better off if each is required to suffer the occasional intrusion from the other,[4] and then extend that principle so that the electromagnetic waves can pass freely across property. In essence the right to receive information then

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[3] Richard A. Epstein, *The Static Conception of the Common Law*, 9 J Legal Stud 253 (1980).

[4] See *Bamford v Turnley*, 3 B & S 67, 83-84, 122 Eng Rep 27, 33 (Exch 1862) (Bramwell).

becomes a new type of property right that is protected against various forms of interference, whether by rival broadcasters who (by analogy to adverse possession) start to broadcast at some later time, or against other parties whose activities jam and destroy radio signals.

The able judge will reach this conclusion because he understands the general principle that a system of private property tends to lead to an efficient deployment of resources that works to the long-term advantage of the public at large. The able judge also understands that such a system will not do so when it rigorously enforces boundary conditions, creating more bargaining and holdout problems than it avoids. It will not do therefore to allow any landowner to prevent any broadcaster from sending signals over his land. Nor will it do to allow one broadcaster to silence another because there is some reciprocal low level interference of signal. A new set of property rights is thus superimposed on an old one to create exclusive rights in resources that have become capable of use only with technological advance. But there is little new in the process. The older common lawyers understood the importance of applying sound principles derived from settled cases to novel situations.[5]

The key question is why rules governing private property (by which I include those dealing with property, contract, and tort) enjoy such great temporal durability in the common law. And the answer is that they depend upon assumptions that hold across a wide range of circumstances and cases. There are certain permanent features of the human condition that are not dependent on technology or on the peculiarities of time and space, and these are largely independent of historical accident and circumstance. It is to these permanent features of the human condition that any sound legal system must respond.

Two conditions come instantly to central stage. First, the scarcity of resources is a constant condition for all societies at all times, no matter how they are organized. There is never enough to go around, and hence the prospect of conflict and disappointment

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[5] See, for example, *Pasley v Freeman*, 3 T R 51, 63, 100 Eng Rep 450, 456 (KB 1789) (Ashurst):

> Where cases are new in their principle, there I admit that it is necessary to have recourse to legislative interposition in order to remedy the grievance; but where the case is only new in the instance, and the only question is the application of a principle recognized in the law to such new case, it will be just as competent to Courts of Justice to apply the principle to any case which may arise two centuries hence as it was two centuries ago . . . .

is inescapable regardless of the rules that are used to determine the production and distribution of goods. Second, the widespread, if not universal, presence of self-interest necessarily follows. Any individual who practices a form of voluntary and unreciprocated altruism will have fewer resources at his command than one who follows the dictates of self-interest. Over time, those individuals with a larger resource base will drive out those individuals with a smaller base until we can expect to see the world dominated by persons with self-interest.

On this view of the world, it makes little sense to condemn individual conduct because it is motivated by an ample dose of self-interest. Instead the central task is to figure out how sound legal institutions can harness that self-interest to produce desirable social outcomes. Both theft and trade are acts driven by self-interest, but they differ in that the former is always a negative sum game (that is, one where the gains to the winner are smaller than the losses to the loser), while exchange is a positive sum game from which all profit.

Given the fundamental distinction between theft and exchange, any legal system must discharge three distinct tasks. The first mission of the legal system is to determine an initial set of property rights from which subsequent bargains can go forward at reasonably low cost. The second mission is to insure that these entitlements once established are protected against various forms of theft—the office of the law of crime and tort. The third mission of the law is to facilitate the voluntary exchanges of property rights—the law of contracts.

To return for the moment to the example of the spectrum, the initial determination of property rights can be determined by a principle of first user, subject to a qualification that allows (reciprocally) certain minimal levels of interference for the benefit of the system as a whole. Thereafter actions for injunctions and damages can be allowed to prevent the use of frequencies that have been allocated to others. Finally, contracts can be used to assign or divide frequencies in order to promote more desirable uses. The spectrum is a resource whose potential necessarily depends upon modern technology. It is also a resource whose proper allocation follows by analogy from the ancient and universal principles of private law.[6]

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[6] See, for example, Ronald Coase, *The Federal Communications Commission*, 2 J L & Econ 1, 18 (1959), with his trenchant observation that the system of markets that he advocates might be described as "a 'novel theory' (novel with Adam Smith)." For a modern

Starting from this view of the common law, it is easy to find those judges whose innovation marks a clear retreat from sound principles of legal analysis. A judge who concludes that contracts between merchants and consumers should be invalidated because of inequality of bargaining power may be creative, but he has made a mistake that works mischief for the ages.[7] Under the guise of innovation, he has substituted a view that bargains should be treated by the same rules that govern the various forms of theft. In other words, he replaces the model of mutual benefit through exchange with a model of exploitation through exchange. This substitution invites an unwanted exacerbation of political class conflict by pitting management against labor, landlord against tenant, lender against borrower, and merchant against consumer. The impulse then becomes to suppress useful bargains, thus slowing the wheels of commerce in ways that promise little long-term systematic advantage to anyone. There is really very little about the events of modern times that tells us whether the substitution of a theft model for the exchange model is right or wrong. The revisionist's argument is wrong because it ignores the beneficial logic of self-interest in trade, and it was as wrong in ancient times as it is today. The introduction of arguments about changed social circumstances operates as a smokescreen that keeps us from larger, more permanent conceptions that animate the basic legal system.

B. The Universality of Common Law Principles

The rules of property, contract and tort characterize much of our common law, but the underlying principles are by no means confined to common law jurisdictions. Because they depend only on a "thin" view of human nature—the twin assumptions of scarcity and self-interest—they travel well across time, space and culture. The contracts and social arrangements by the use of these legal rules will differ, but the legal rules that best facilitate the emergence of the strongest social order are largely invariant from place to place.

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defense of a property rights regime in the spectrum, see Jonathan W. Emord, *Freedom, Technology and the First Amendment* chs 12-14 (Pacific Research Institute for Public Policy, 1991).

[7] See, for example, *Williams v Walker Thomas Furniture Store*, 350 F2d 445, 449 (DC Cir 1965). The source of much of this mischief is Friedrich Kessler's elegant but mistaken article, *Contracts of Adhesion—Some Thoughts About Freedom of Contract*, 43 Colum L Rev 629, 640-41 (1943), which contains the implicit but misguided analogy between a capitalist firm and a fascist state during the height of World War II.

I began my academic studies as a fledgling Roman lawyer and have long been convinced that the myriad of differences between the Roman and the common law are best understood as matters of detail rather than as matters of fundamental logic. There are divisions of property, contract, and tort in both systems, and while there are some small differences on matters of classification, or in default rules for damages, there is very little in the legal rules of one system that makes them inoperative in a separate legal culture.[8]

Japan, for example, adopted the German Code shortly after the Germans promulgated it,[9] and there is little reason to think that this Code did not serve the needs of commerce in a society whose major historical attribute had been its self-enforced isolation from Western Civilization and its cultural norms. The Roman law of sale, for example, would be perfectly serviceable in our modern environment given its absence of formalities and great flexibility—attributes that allowed it to evolve to meet the requirements of international trade. The ostensible differences to which comparativists normally gravitate are studied for their academic difficulty and interest, not for their intrinsic importance to the overall operation of a legal system.

The basic point about the private side of comparative law has been made well by Saul Levmore in a series of articles about diversity and uniformity of legal rules across separate legal systems.[10] His conclusion is that uniformity arises on important questions where the costs and benefits of a legal rule are clear. Diversity arises on difficult and elegant points of law where the costs and benefits are hard to trace. Levmore illustrates the basic point with the eternal triangle of property law. A owns property which is stolen by B, who then sells the property to C who purchases the goods in good faith, i.e., without knowledge of the defect in B's title.[11] What ought to be the remedies among the three parties? One could look far and wide across legal systems and find none that takes the position that the thief, if found and if solvent, should be able to keep the sale price, leaving A and C to fight over the goods. The arguments about the destructive force of theft are, at an intui-

[8] See Barry Nicholas, *An Introduction to Roman Law* 206-07, 226-27 (Oxford, 1962) for evidence of how the common features of the Roman and common law systems, especially on critical matters of classification, outweigh their differences.

[9] See Konrad Zweigert and Hein Kotz (Tony Weir, trans), 1 *An Introduction to Comparative Law* 360-61 (North-Holland, 1977).

[10] See, for example, Saul Levmore, *Variety and Uniformity in the Treatment of the Good Faith Purchaser*, 16 J Legal Stud 43 (1987).

[11] Id at 45-49.

tive level, so powerfully felt that no legal system is prepared to make the common thief the favorite of the law. No contingent circumstances and local variations have to be taken into account in making this judgment.

Unfortunately, in most cases the thief (if he can be located) does not have the proceeds of sale. The only thing that can be done with him is to inflict some sort of punishment—be it by jail, hard labor, torture, death—by way of deterrence against repetition of the practice by him and by others. Yet even after that punishment is introduced, there is still the question of who should bear the loss, A or C. There are any number of approaches to that question. One could concentrate on the location of paramount title, which would tend to favor A, or the ability to prevent the loss, which would tend to favor C. One could ask what either A or C would choose if located behind the veil of ignorance;[12] or ask whether the same rule is appropriate for negotiable instruments as is for chattels as is for agricultural products; or ask whether it makes a difference whether C purchased in a private sale or in an open market. The balance of convenience between all these choices is close, for second-best questions—those that arise because A and C cannot find the thief, B—often do not admit of decisive answers. There may be some local variations that move a culture in this direction or in the other, but these variations are very hard to identify, and of little consequence to the overall efficacy of the system.

In the end it is clear that loss-shifting rules are limited in their potential to handle this problem, for whatever additional incentives are placed on A are necessarily removed from C and vice versa. It is quite likely that the best solutions are those that try to avoid the problem by making it harder for B to steal, as with a better police force, or for C to claim the status of a bona fide purchaser, as with product identification marks or recordation that gives notice to the world of prior possession. The difficult question therefore is the one that generates many subtle variations, but these variations are no greater across time and distance than they are within a stable culture. The variation arises largely from the difficulty of getting a dispositive answer to the question as a matter of first principle, given the thin conception of human behavior (egotism, greed, self-interest) that all societies use to analyze the underlying issue. No revelations derive from the comparative ap-

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[12] See John Rawls, *A Theory of Justice* 136-42 (Harvard, 1971).

proach that are not available to persons who bring a powerful analytical tool kit to domestic problems.

II. First Principles and Constitution-making

This same approach—one that posits the universality of first principles—I think applies to the far more difficult problem of constitution-making, where the problems of scarcity and self-interest require a society to face far more epic forces than those it confronts with the eternal triangle of the common law. The basic problem is, and always will be, as follows: a market that operates on voluntary transactions will not be able to generate the initial set of property entitlements on which subsequent transactions depend, nor will it be able to enforce and protect the entitlements that are so generated. Some uniform approach to these questions must be developed, and it must be enshrined in a constitution or other permanent political institution. Thus, to overcome the risk of chaos, we have to be prepared to run the risk of tyranny.

The question then arises: Is there something that can be done to reduce that risk to acceptable levels, just as an investment in an expensive recordation system might pay for itself by enhancing the security of title? The basic answer to this question has to be yes. But then the further issue arises: What are the optimal set of precautions to create the largest net gain from government (i.e., the ability of government to provide for useful services, less the risk of abuse)? Unfortunately, the catalogue of devices that are known for this purpose is relatively limited, and all of them will have to be tried in some form in Eastern Europe, just as they have been tried in constitutions that have succeeded and failed elsewhere.

A. Separation of Powers

The first of these devices, separation of powers, is designed to make it more costly to achieve the minimum coalition necessary for political action. In ordinary private transactions, any set of rules that throws external barriers in the path of voluntary exchange is normally and properly regarded as a mistake. But in political markets the converse is true. Private parties do not have the power to tax or to regulate strangers, so the externalities that they create from consensual transactions (subject to an exception for price fixing and similar arrangements) are usually *positive* because they create additional opportunities for contracting to the strangers to the transaction, given the increased wealth of both A and B. As all parties are presumptive winners, there is no case for public restriction on ordinary private market transactions.

Within the political arena, however, majorities can bind minorities, so that the transaction that produces net gains for the members of the winning coalition may produce dramatic losses for the outsiders. Presumably, if transaction costs were low enough within the legislature, the outsiders might buy themselves a charmed place in the inner circle, and thus allow political markets to replicate the widespread gains derivable from economic markets. But it is unreflective optimism to conclude that political markets are capable of clearing with anything like the efficiency of competitive economic markets. The rules for separation of powers recognize the outsider's risk from exclusion and thus place greater obstacles in the path of political agreement. Separation of powers is a highly imprecise device, and the best that we can expect is that it will act as an imperfect filter to keep out legislation that has slender actual majorities (and hence is likely to do more external harm), while letting through legislation that commands greater majorities.

One should not overlook the fact that this filter has serious limitations, however. Suppose there is a small minority that vigorously opposes some legislation, and a majority that has modest sympathy for it. It is quite possible that the small group's skills, influence, and tactics will not allow it to overcome the majority even if the small group's private losses are far greater than the gains to the other side; the political system fails to account for the intensity of individual preferences. Indeed, dubious legislation has passed too many times in this country under a system of separation of powers for anyone to believe that the device—however critical to the success of the overall system—will be a panacea against all legislative evils. Separation of powers, then, is a doctrine that gains its place not because it stops all abuse in its tracks, but because it provides some protection whose anticipated value is greater than its cost. There is no perfection from this political device—only a chance to shorten the odds of shipwreck in the political order. Politics, like poker, is a game of edges.

B. Federalism

When the attention turns to federalism, the stakes are as high for Eastern Europe as anywhere else. In the United States, the problems of federalism were the problems of regionalism within a common language and a common culture. While from time to time these conflicts have created bitterness and local tensions—for example, the nineteenth-century issues of the tariff, or the twentieth-

century question of the western lands—only once in our history did these conflicts erupt into full-scale violence, and that was during the Civil War.

Eastern European nations will not be so lucky as we, for even though their territories are far smaller than ours, the racial, linguistic, and national diversity within their tight boundaries is in many instances far greater. Even the prospects for geographical separation within a federation are limited because there are often minorities nested within minorities, or widely diffused throughout a larger population, so that short of migration any set of boundaries will leave at least some group exposed to the depredations of its historical enemies. The United States (unlike Canada whose federation may soon unravel over the status of Quebec) has long had the advantage of a dominant single language that furnished the basis for a common internal market in trade. In contrast, the diversity and separation of the Eastern European languages will be a barrier for both trade and governance. Within the United States, the exact lines of the division are not that critical. It is enough to create jurisdictions that must compete with each other for business in a world in which exit rights are reasonably secure. But with Eastern Europe, the choice of lines is critical, because there is reason for concern if an ethnic group spans two states within a federation, or if a state contains two equal groups. Either situation can easily prove explosive.

The logic behind federalism posits that one of its advantages is that it allows for a fuller satisfaction of separate tastes.[13] This is indeed true to some extent. Take, for example, nation A, where there are 120 people of type X and 80 of type Y. It might be possible to divide the nation into two states, one of which contains 100 of X and 20 of Y, and the other 60 of Y and 20 of X. In the first configuration (before the division), majority choice will allow for the satisfaction of 60 percent of the total, while federation allows for the satisfaction of 80 percent of the total. But so long as the separations are partial and not complete, this justification for federalism is too pat and over-optimistic.

Before the federation is in place, it could well be that each group is able to hold off the other, perhaps because of some supermajority provision. After the separation and federation, it is possible that 40 people (or 20 percent of the nation's total popula-

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[13] See Michael W. McConnell, *Federalism: Evaluating the Founders' Design*, 54 U Chi L Rev 1484, 1493-94 (1987) (review of Raoul Berger, *Federalism: The Founders' Design* (Oklahoma, 1987)).

tion) will be subject to total confiscation or denial of ordinary civil rights. Thus, a two-thirds provision that protects against the abridgment of fundamental rights at the national level will prove unavailing once federalism and division have taken place.

Nor is federalism the perfect solution when the number of groups within a nation is increased to three or more, because the problems of local oppression and domination do not disappear simply because more groups are subject to a common federal government. All these difficulties do not suggest that federalism should not be tried to alleviate ethnic tensions, for there is no clearly better alternative. The problem is not with constitutional strategy but with our high expectations. The competition between governments created by federalism exists only over certain persons and certain activities: it affords a substantial protection to new businesses that have a choice as to where to locate their plants. But it does not afford protection to the owners of land, which is immovable, or to political minorities for whom the cost of exit is, or is made by regulation, prohibitive.

In addition to these problems inherent in the federalism principle, one must consider the fact that federalism has fewer obstacles to overcome in America than in Eastern Europe. Paul Johnson has catalogued at length the major dislocations and atrocities that occurred when the map of Europe was redone at the conclusion of the First World War, with the breakup of Austro-Hungary, the realignment of other borders, and the births of new nations.[14] Old rivalries that had been kept in check within large nation-states surged to the fore. We now risk the same difficulty in Romania (with the Hungarian minority) and in Yugoslavia (with its eight distinct nationalities).[15] Once separation takes place, there is no assurance that bloodshed will not follow. In the American context, any old set of lines will do most of the time, for no matter how the lines are contrived, South Carolina and Montana will not a have a common border. But in Eastern Europe, the stakes regarding the boundaries for federation, or indeed for total separation, are much higher.

The current preoccupation in Eastern Europe is with the problem of ethnic conflict. It is in a sense not surprising that this issue should have displaced the transition from a planned to a

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[14] Paul Johnson, *Modern Times* 37-40 (Harper & Row, 1983).

[15] See Chuck Sudetic, *With Yugoslavia in Turmoil, Macedonia Holds First Free Election*, NY Times 16 (intl ed, Nov 11, 1990). With at least eight separate regions, there appears to be no reason why Yugoslavia should be kept a single nation.

market economy as the central stumbling block in the making of Eastern European constitutions. The control of state monopolies has to take a back seat to the prevention of potential bloodshed.

C. Constitutional Protections of Individual Rights

So we come to the last of our possibilities, the protection of individual rights under a constitution, including those of speech, property, and religious freedom. The logic of a system of liberty is that collective decisions are difficult to make, and often unnecessary. Whether we eat pizza or tacos for lunch should not be decided by committee vote. Each citizen can make his own choice. Better it is therefore for the state to carve out many separate domains in which single persons have full power of choice than it is for the state to create larger domains in which many persons share the decisionmaking power under some voting rule. I think that it is inconceivable that we should want religious beliefs and practices to be chosen by collective decision. While there is today widespread acceptance of the vital role of freedom of choice, and the importance of self-realization in connection with intimate personal associations, I see no reason why the same logic should not apply to associational preferences that apply in all domains, including the economic. There are probably as many people who achieve self-realization (as they define it) through work as through marriage, and the state should not take it upon itself to decide which forms of association are worthy of respect and which are not.

The principle of limited government should be of special usefulness in Eastern Europe where the divisions between people are so deep that *any* collective decision is likely to leave a sorely aggrieved minority. The animosities of centuries are not likely to disappear with a few days or weeks of earnest constitutional conversation. It is far better therefore to promote a regime of individual liberty and freedom of association, so as to avoid the dangers associated with extensive forced interactions. So long as government power is used to keep people apart until they choose to come together, there is a greater chance that people of fundamentally different preferences can live together under a single government than there is if the state is given extensive powers to bind, regulate, tax, and coerce by collective decision. Indeed the greater the internal disparity, the more critical it is to have a small list of core government functions on whose discharge all can agree. As geographical federation has only limited use in the Eastern European checkerboard, small government at all levels allows economic and social separation to mitigate ethnic conflict when geographical sep-

aration is not possible. Eastern Europe will prosper from a strong dose of freedom of contract and association. It should be especially wary of employment discrimination laws.

Still I am not sanguine about the prospects of a system of liberty. There are too many people who will wish to settle old scores by whatever means that are available to them. There are too many people who believe that they are clever enough to rig a system that makes their own lofty visions of the just society politically obtainable. Most critically perhaps, working out the system of constitutional liberties, as our own history has shown, is far more complicated than the brief thumbnail sketch given above suggests.

All constitutional liberties start life as absolutes. They end life, however, as the first stage in a balancing process—a process that gives no clear guidance as to what exceptions should be allowed, what qualifications should be heaped upon the exceptions, what burdens of proof should be assigned, and who should decide whether the rights have been abridged or respected. In our own tradition, we have embraced a problematic distinction between preferred freedoms (speech, and until recently, religion[16]) and ordinary economic liberties, where very low standards of justification are now required to legitimate state action. A system of protected liberties is far from self-defining and self-enforcing, and we have made, in my view, serious mistakes in relaxing the constitutional guarantees for economic liberties and property rights. Today, mere regulation passes constitutional muster, even though its broad application means that it often will have major adverse consequences. The police power covers just about any interest that one could divine, including protecting individuals from the consequences of their own voluntary contracts. We have been able to survive this set of constitutional blunders because our political infrastructure, although flawed, still manages to impose some restraints on government action. But the costs to domestic prosperity have been high nonetheless.

Within the context of Eastern Europe, property and economic protections are critical to the ability to turn nations and economies around from central planning to private ordering. The key elements are stability and permanence of the property rights structure. There is surely a general belief in most Eastern European countries that selling off nationalized businesses is the first step in

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[16] See *Employment Division v Smith*, 110 S Ct 1595 (1990), and Michael W. McConnell's critique, *Free Exercise Revisionism and the* Smith *Decision*, 57 U Chi L Rev 1109 (1990).

an orderly progression to a viable market economy. But while there is consensus today on denationalization of industry, there is little consensus on the steps that will—and ought—to follow these sales. Most concretely, the Eastern European countries, preoccupied as they are with the status of ethnic divisions and minorities, have failed to make state regulation of economic affairs subject to any form of constitutional discipline.

Given the strong socialist tradition that lurks within the interstices of the older communist order, one cannot expect the public (through its legislatures and its courts) to conduct a radical transformation of society and to embrace ardently an intelligent system of laissez-faire capitalism. Quite the opposite is more likely. There will be the predictable calls for prudence across-the-board; a wait-and-see attitude will take hold with respect to the general economic reform that follows the initial prioritization. And that call could be fatal to any systematic improvements in social well-being.

III. The Failure of Gradualism

A. The Time Element

In dealing with the questions of privatization, it is important to be aware not only of the perils of rash actions, but of the perils of prudence as well. The attempt to run a political "experiment" with market institutions may be the very decision that defeats the successful transition to markets in the first place.

One critical element in understanding the operation of markets concerns the time horizons under which they operate. If X is thinking of starting a business, the first question she will have to ask is whether she will be able to recoup in the future the front-end investment that she is required to make today. Where businesses require an extensive commitment of time and labor, the period over which the recoupment could take place can be quite long, perhaps several years, or even a decade or more. The owner is prepared to wait a longer period of time before recouping her original costs when the legal environment is stable, when the regulatory structure is predictable, and when the tax burdens are ascertainable. When American companies invest in unstable countries, typically they will only look at investments that pay their way in three years or less; when they go to established Western Europe economies, they will take a very different view of the time horizon, accepting a lower per-period rate of return because they are confident that there will be a larger number of periods over which the investment can be recovered.

So what is the situation in Eastern Europe? Without the strongest possible constitutional guarantees of property rights, and perhaps even with them, potential investors will have to take a short-term view of their investment prospects. They will choose only those projects that yield very high short-term returns. The adoption of that point of view will then lead the Eastern Europeans to regard the investors as mere speculators. Popular resentment will grow because of the excessive returns that capitalism promises the few at the expense of the many. There will be a strong demand for leveling and for countermeasures, and these will paradoxically be seen to have justified the original decision to hold off on investment unless extraordinary returns are promised.

If the environment were otherwise, investors would undertake more projects, some promising lower rates of return. Economic activity will do better precisely because the political institutions of the state have crossed their Rubicon by giving permanent constitutional protection to property rights. There will be fewer cases of extravagant return and broader participation in the overall market. Thus the very effort to constrain the nature of the market experiment to a limited period of time distorts the results that the experiment itself now yields, and guarantees its failure. The effort to temporize on the shift to markets increases the likelihood of failure.

B. The Atmosphere of Crisis

A related phenomenon that may doom private ordering in Eastern Europe has to do with the fact that those nations now face a crisis of monumental proportions. When matters are truly desperate, it may be possible to forge a coalition that will take radical steps to avoid a wholly untenable situation. If markets are thought to increase the levels of overall production, people could be persuaded to put aside their fascination with regulation and redistribution in order to survive. But once the situation improves—once the people begin to take stock in the changes that have occurred—there will be a tendency for some people to argue for the short-term distributional gain over the long-term productive one.

No set of legal institutions can prevent this squabbling from happening. However, an awareness of the risk may encourage the nations to go "cold turkey." Indeed, an attitude of "there's no going back" drastically improves the chances of success. The situation in Eastern Europe is so desperate in so many nations that all the eggs have to be put in one basket.

C. Monetary Policy

There is an additional element to this theme that bears some notice as well. It is not enough to have a stable system of property rights unless there is also a stable currency, a task that is peculiarly difficult to discharge for governments under siege. Again, there is a good deal that can be learned from the American experience. During the Great Depression, when the currency was allowed to deflate by some 30 percent, the shifts that took place did more than simply change the relationship between money and goods. It was not as though everyone had fewer dollars but their economic net worth in real terms remained the same. Instead, the deflation worked a substantial redistribution of wealth between debtors and creditors in ways that prompted massive social dislocations.

A simple case illustrates the general theme. Suppose that a bank lends a farmer $1,000 to be repaid in five years. If the value of the currency is deflated by 50 percent, then the $1,000 owed becomes in real terms a debt of $2,000, the additional burden of which may spell ruin for the farmer, even as it creates a windfall to the bank. But even that windfall may prove to be a mixed blessing if the bank has borrowed from some other party. When its farmer-debtor defaults, the entire structure can fall like a row of dominoes. The instability here is in fact no different from that which would occur if the state simply announced that the farmer owed the bank an additional $1,000.

What is true of a lending arrangement is also true of every other form of private contract, including those for the sale of land and goods. If it is thought to be unpardonable government action to change the quantity term of a contract, then so too is it an unpardonable error to change the price term. What holds for deflation holds for inflation as well. The point here is an old one, but it bears retelling in this context, given that the temptation to inflate a currency to reduce government debt will be strong for all countries in the Eastern bloc, just as it is in the United States. A stable system of property rights and a strong system of contractual enforcement counts for little if the state currency is subject to political manipulation. At the very least all local currencies should be freely convertible in world markets. Otherwise there is no effective, anonymous and impartial check against political tampering with the currency, and there is no way to induce foreign capital to come into a country from which it cannot at some future time freely exit. The creation, therefore, of a system of property rights does not depend solely upon adopting a sound set of rules of property, con-

tracts and torts. It depends on a set of sound public institutions as well.

CONCLUSION

This somber assessment of prospects thus returns us to my original theme, All Quiet on the Eastern Front. In essence, I think that it is possible to give this assessment based on only the most general features of political life. The material about separation of powers, federalism, and vested rights all depend on the kinds of facts with which we are all familiar. The concerns with faction, self-interest, and ethnic and national rivalries are hardly the stuff of great originality. But because the transitional problems are so intractable, it is possible to maintain this paradox: what will happen in Eastern Europe will amaze, astound, and largely disappoint. And these troubled results follow inexorably from general political principles that are—or at least should be—familiar to all students of constitutional government.