

Is the Rule of Law Friendly with Exchange Activities?*

Rhee, Sung Sup**

〈Contents〉

- I . Introduction
- II . Imperfectness of Institutions and Relation Exchange
- III . Legal-Institutional Module of Relation Exchange
- IV . Friendliness of CCK Decisions (1988-2003) with Exchange Activities
- V . Concluding Remarks

Abstract

Is the rule of law friendly with exchange activities? In this research, attention is laid on the imperfectness of institutions. Relation exchanges, which arise from imperfectness of institutions, enable the economic analysis to stretch out from value exchanges in the market to the territory of relation exchanges. By recognizing value exchanges in the market as special cases of relation exchange where property rights are perfectly secured, all daily activities of individuals become part of relation exchanges and become objects of economic analysis. Hence, institutional dimension become put in place as independent axis of economic analysis. Now, it becomes possible to identify the order of relation exchange as social order. For instance, it becomes possible to analytically draw out the role of third party, e.g. government, from Hobbesian social contracts, which performs to secure the stability of social order. The building of theoretical groundwork as such renders it possible to recognize institutional phenomena like morality codes, law, public administration, and other social norms, which uphold stable operation of social order, in the analytical structure of relation exchanges.

* This paper was presented at 2011 Institution and Economics International Conference held at Fukuoka, Japan, on August 17-18, 2011.

** Professor, Soongsil University, email: rheess@ssu.ac.kr

Analytical foundation has been built to determine if such legal institutions are performing friendly with exchange activities. Introduction of two dimensional concepts, i.e. existential modules and operational modules of legal institutions, and through their intercross, rendered it possible to construct conceptual categories for legal-institutional modules of relation exchange order. Each decision of the CCK(1988–2003) was assigned to one of 45 conceptual categories and pigeonholed as such. Proactivity or retroactivity of each decision was determined according to conceptual categories of the cell in the module matrix. The outcome of research seems to establish the proposition 'the rule of law cannot but be friendly with exchange activities.'

Key Words: *Imperfectness of institutions, Value exchanges, Relation exchanges, Rule of law, Friendly exchange activities*

I . Introduction

Is the rule of law friendly with exchange activities? The question and laying theoretical groundwork upon which to draw out analytical structure to answer the question are the gist of this research.

Hayek raised the same question in *Law, Legislation and Liberty* (Hayek 1982) and presented spontaneous order as answer to the question. Although Hayekian answer unveiled the direction leading to the answer to the question, two essential problems challenge and reveal the intractability of the problems.

Firstly, the concept of spontaneous order is abstract and lacking in concreteness. Especially, the link between legal institutions and spontaneous order is neither specific nor concrete. This research presents ways to add concreteness to the link between legal institutions and spontaneous order.

Secondly, theoretical interface between Austrian approach of Hayek and orthodox analytical structure are lacking. This is a fundamental problem of economics. In Austrian approach, concreteness is lacking in legal institutional modules. In orthodox economics, theoretical structure to recognize institution in analytical architecture is not prepared. New institutional economics approach is attempts to interpret institutional operations with analytical tools of orthodox

economics. It does not offer institutional dimension to analytical structure of orthodox economics as new analytical axis.

In this research, it is underscored that orthodox economics fail to recognize the role of institutions in economics analysis because institutions are not conceived as independent autonomous factors of analytical theory, but simply treated as external environmental factors. Relational contract theory recognizes lock-in effects by measuring transaction costs in theoretical structure of orthodox economics and attempts to explain ex post monopoly relations (Williamson 1985; Hart 1987). However, it is existential reality that transaction cost measures become rendered unstable through interactions between changes in institutional environments and analytical structure of orthodox economics. Unstable transaction cost is essential reason why orthodox economics approach is bound to fail in recognizing the substance of institutions (Rhee 2010).

In this research, the imperfectness of institutions (Eggertsson 2005; Rhee 2010) is recognized, which helps build interface connection in analytical structure between Austrian approach and orthodox economics possible.

In this research, existential modules of legal institutions of relation exchange order *modus vivendi* as well as operational modules *modus operandi* will be distinguished. We will see, Table 1 (Legal-Institutional Modules of Relation exchange Order) is the outcome drawn out from the intercross of two modules.

In this research, 29 decisions of the Constitutional Court of Korea (CCK in short) (1988-2003) are classified and investigated according to the concepts of modules of Table 1. The research leads to the conclusive proposition ‘the rule of law is friendly with exchange activities.’

Section II introduces the logics and reasoning to draw out relation exchange concepts from imperfectness of institutions. Section III recognizes the possibility to establish social order for relation exchange activities. Existential modules and operational modules of legal institutions are drawn out from social order. In these steps, the friendliness of legal institutional changes with exchange activities will be judged according to conceptual categories of legal institutional modules. In section IV, 29 cases of CCK decisions (1988-2003) will be classified according to the module schemes of Table 1. The friendliness of

CCK decisions (1988-2003) will be assessed. Section V summarizes the research and presents conclusions.

II. Imperfectness of Institutions and Relation Exchange

In legal definition or at implementation steps, institutions are distinguished by the attribute of imperfectness (Eggertsson 2005). Property rights are special types of institution so that they share the fundamental attribute.

Plenty of institutions stipulate on property rights; laws, precedents, regulations, enforcement ordinance, bylaws, etc. Nevertheless, such property right as to define perfect ownership in every situation is practically not possible to set out. Taking steps of law enforcement into consideration, the difficulty redoubles (Dworkin 1986).

Innumerable cases of lawsuits under deliberation in civil courts vindicate the imperfectness. In real life, more cases of disputes exist, which are not even lodged for trial in the court. Absolutely, property rights, not to mention institutions in general, are imperfect by themselves. Especially, the imperfectness of property rights exacerbates in case of brand-new economic activities, e.g. intellectual property rights.

If the imperfectness of institutions, especially that of property rights, are taken for granted, how exchange activities come off?¹⁾ Clearly, exchanges cannot be completed merely by value exchanges²⁾. In the condition of imperfect property rights, such personal behaviors that complement value exchanges and complete exchange transaction tends to develop (Rhee 2010).

¹⁾ In this research, exchange activities are closed up because they are considered the core of all economic phenomena. Benefits of economic activities arise fundamentally from exchanges. Exchange helps locate division of labor, i.e. specialization. Specialization is the source of productivity increase (Smith 1776).

²⁾ Value exchange indicates exchange transaction, which takes place in market by means of price. In this research, value exchange is compared with relation exchange, which will be introduced soon after. Relation exchange carries out by means of trust, not by price.

For instance, behaviors intending to build trust relations tend to come out (Fukuyama 1995)³⁾. Attempts arise to make up for imperfect property rights by building trust relations among individuals or in the activities of social constituents (cf. limited-access natural states: North, Wallis, Weingast 2009). Subsequently, such structure of social order as to set out effective exchange order, which is upheld by laws and public administrations that are essentially built upon trust relations, is to set out (cf. open access order: North, Wallis, Weingast 2009).

Upon accepting the premise of imperfectness of institutions, it is opportune to introduce discussions on the concept of relation exchange in order to draw out spontaneously grown institutions like morality codes, men-made institutions like laws, public administrations, and varieties of social phenomena to the fore of theoretical analyses of economics as essential elements (Rhee 2010). This research lays base structure upon which to lodge morality codes, laws, public administration, and various social phenomena as essential elements of theoretical analyses.

Definition 1 (Relation exchange): Relation exchange indicates exchange activities of the objects, upon which property rights are not established, by means of trust as medium of exchange among individuals or social constituents in the process of their efforts to seek individual interests.

Here, trust is comprehensive concept, which embraces all of friendship, fraternity, affection, colleagueship, solidarity, etc. Relation exchanges indicate group activities, alumni relations, friendships as well as activities to forge trust among individuals or to secure customer credibility, etc.

Exchange activities are value exchanges and relation exchanges as well.

We, who were trained by the tenets of orthodox economics tradition, are familiar with the concepts of value exchange, but are not accustomed to the

³⁾ In this research, trust is more comprehensive concept than that of Fukuyama (1995). Trust indicates not only the concept of Fukuyama (1995), but also trust feeling arising from friendship, fraternity, solidarity, affection, etc.

concepts of relation exchange. Value exchanges in the market or market exchanges take place to the objects, for which property rights are established, whereas relation exchanges appear to those objects, for which property rights are not established.

In the value exchanges of the market, goods are measured in value. Price plays the role as medium of exchange at the same time. However, in relation exchanges, the objects of exchange may be measured in value, but price is unable to play the role as medium of exchange.

Trust takes the role of price and performs as medium of exchange. When having meals with friends, going hiking or exchanging information, we make friendships and forge trust and expect rewards from such trust relations. Rewards may be security of safety in opportunistic rivalry condition, information gathering or favored treatment in business talk, etc.

In relation exchange, institutions, i.e. like trust, appear not as backdrop condition, but appear to perform a role as essential element of theoretical analyses when being conducted on exchange activities⁴⁾. Relation exchanges take place by means of trust as medium of exchange. Trust becomes forged (or eroded) during the process of exchange activities.

In a human society, relation exchanges remain extant from the beginning. Relation exchange is most fundamental action of human lives in a society⁵⁾. Even in the ages of primitive life, human beings build private relationships among individuals to reaffirm trust by exchanging goods, affection, friendship, solidarity and pursue the security of personal life in materialistic and psychological sense. They do not hesitate to pay psychological, temporal, and material costs in order to build relationship networks, by means of which to exchange trust among individuals or groups.

⁴⁾ The fact that trust appears as essential element of analysis in the theoretical structure of economics indicates that the analysis cannot be conducted with price p and quantity q only. It indicates the need to include institution i as essential element of analysis. In Rhee (2010), the former is named System(p, q) and the latter System(p, q, i). Rhee (2010) illustrates that System(p, q, i) is entirely different world from System(p, q).

⁵⁾ Home is the community, the management of which is upheld by relation exchanges only, without the assistance of value exchange.

There is no essential change in such human behavior even recently in post-industrial age. The social life, which is mounted upon trust as bedrock, is elementary grid of human society⁶⁾. People gladly pay economic costs or spend time to attend alumni association.

Institutional features, by which trust comes off to function, change according to societal difference and age of times. Relational networks of types peculiar to developing society, which may be close to cronyism, distinguishes from relational networks of advanced-societal type, which is anchored in trusts upheld by principle of integrity. The former is costly as the sustenance of trust relations is deterred by trial and errors and incurs costs.

Market exchange, i.e. value exchange, arises from the underpinning of relation exchanges. If property rights are properly established so that the valuation of objects exchanged is objectively assessed, the building of trust relations complementary to exchange activity becomes unnecessary. Exchanges attain efficiency and do not incur costs to uphold relation exchanges.

However, the circumstantial condition does not allow appropriate establishment of property rights for the objects of exchange, value exchange cannot be realized. The attainment of exchange requires complementary setup of trust relations. Price is not used as medium of exchange. Hence, the exchange does not necessarily require parity of values between the goods exchanged, which is distinguished from market exchange.

Market (value) exchange and relation exchange are not exclusive occurrences, but makes an integrated composite, which establishes complementary relations and builds integrative economic order (Rhee 2010). Besides, this integrative economic order is supported by morality codes, laws, public administration, and various social phenomena as essential composite factors (North, Wallis, Weingast 2009).

⁶⁾ In this research, trust is the comprehensive concept, which includes friendship, fraternity, affection, collegueship, solidarity, etc. In this regard, it is distinguished from traditional definition as in Fukuyama (1995).

III. Legal-Institutional Module of Relation Exchange

1. Order of Relation exchange Activities

Imperfectness of institutions opens gateway to the world of entrepreneurship and secures foothold for entrepreneurship of businessmen (Rhee 2009). It is entrepreneurs who introduce innovative business models, by which to create such business conjuncture as to break through imperfectness of institutions (Chandler 1992). Therefore, we can possibly compare different institutions to determine which institutions are more likely to trigger active transactions or exchange activities when being combined with specific conjuncture of environment.

This approach, when compared to the hypotheses which uphold the argument that institutions make influence on economic development (North 1990; Acemoglu, Johnson, Robinson 2004), is differentiated by a new attempt, i.e. intermediation of relation exchange activities in steps of linkage from institutions to economic development.

Market (value) exchanges take place to the extent that property rights are enforced for the objects on which property rights are established (Demsetz 1967). Hence, the institutional changes, which contribute to the erection or establishment of property rights, are laying ground on which to transform relation exchanges into market exchanges to that extent.

For instance, if a decision of the Constitutional Court clears up the contentious points of property rights issue, enhances clarity and reinforces ground for better performing property rights, the value exchanges of objects in the market will be realized with less assistance of relation exchanges. To that extent, exchanges become more efficiently carried out and invigorated. In a nutshell, judicial reviews of the constitutional court tend to lay institutional changes and stimulate exchange activities.

Institutional changes which establish property rights stimulate exchanges by transforming relation exchanges into value exchanges. In contrast, institutional

changes which erect trust relations tend to activate exchanges by enhancing efficiency in relation exchanges.

If institutional imperfectness is conceived and if relation exchange is set in place, unlike in the theoretical structure of orthodox economics where value exchange only exists, the institutional module of morality, which can classify spectrum of difference in relation exchange by measure of trust, as well as institutional module of law emerging thereupon, is able to appear in the analytical structure of exchange activity.

The legal-institutional modality follows evolutionary process of institutional change. Variety and difference may exist in the ways of conceptual construction or classification conduct when to determine legal-institutional modality.

How are we to devise legal-institutional modality of exchange activities?

In this research, the legal-institutional modality, which will be introduced later, will be used when to assess the friendliness of decisions of the Constitutional Court in Korea in relation with exchange activities. For this purpose, we need to understand the existential being of the order for exchange activities. Hayek called it spontaneous order (Hayek 1982).

In order to gain the comprehension on the analytical modality of institution, which imbeds existential concreteness, we need to understand the module of exchange order. Relation exchange seems to perform as essential role at this juncture. Market exchange is no more than a specific type of relation exchange.

Property 1 (Market Exchange as Specific Case of Relation exchange): Once relation exchange is considered as fundamental element of exchange activities, value exchanges in the market become specific case of relation exchange for the goods, the property rights of which are securely established.

Property 1 indicates the recognition of exchange order as composite of relation exchanges. In relation exchanges, the costs, which are required to sustain trust, should be paid to carry out the activities of relation exchange. If property rights are perfectly set in place, relation exchange will change to value exchange so that costs to sustain trust become unnecessary⁷⁾.

Proposition 1 (Relation exchange Activity): Taking relation exchanges for granted, all exchange activities may be perceived as activities of relation exchange. Value exchange activities in the market may be conceived as relation exchanges for the goods, the property rights of which are established.

[Proof]

Activities of relation exchange are the exchange activities, which take place with the use of trust as exchange medium. Value exchange in the market is essentially not different from relation exchange. What is exchanged is objectively-measured values of the goods in the value exchanges.

Value measure is not different from trust-keeping. For value exchanges to take place, property rights should be set in place in advance. Measuring of values is allowed only when perfect trust is erected. The costs of trust-sustaining is nil or insignificant in value exchanges when compared with cases of relation exchange. Value exchange may be considered special type of relation exchange.

The procedure where value exchanges take place requires spending of costs, i.e. transaction costs. It is the costs that arise in the procedure where demands and supplies encounter, the value being assessed, and the exchange price being determined. It is the costs which are required to set up and operate market institutions. Leaving the costs of establishing market institutions out of consideration as sunk cost, operational costs of market institutions in value exchange are not large in itself and remain in stable boundary. They are not such a variation factors that essentially repudiate the application of relation exchange as integrating concept which uses trust as medium of exchange. In other words, all exchange activities may be conceived as activities of relation exchanges. □

Property 2 (Order of Relation exchanges): The order of relation exchanges means to indicate the social order, which is built upon activities of relation exchanges.

⁷⁾ Here, property rights are comprehensive concept, which includes property rights as well as contracts.

Since relation exchange is fundamental propensity of human behavior when imperfect institutions are assumed, what is meant by order of relation exchanges indicates the possibility of constructing social order which builds upon activities of relation exchange. This order of relation exchange is not different from Hayekian spontaneous order (Hayek 1982).

Proposition 2 (Social Order Attributes Determined by Third Party Norm): Social order of relation exchanges unfolds a variety of attributes differences, the spectral changes of which are determined by institutional factors, e.g. third party norms⁸⁾.

[Proof]

Property 2 implies that once imperfect institution is presumed, relation exchange activities sets out foundation for the building of natural social order in human society. It is not different from Hayekian spontaneous order (Hayek 1982). Third party norms, either morality codes, laws or other module of institutions, determine attributes difference of such social order. It could be Hobbesian dictatorial social order, which perceives ‘war of all against all’ as state of nature (Hobbes 1651). Or it could be Lockean social order of civil society (Locke 1690). Variety of social orders with distinctive political or operational attributes is determined by institutional composition. Institutional change lays impacts on the attributes of relation exchange activities. Hence, eventually on attributes of social order. □

Relation exchange is fundamental propensity of human behavior. Value exchange in the market is not different from relation exchange, but a special case thereof where property right is perfectly established for the goods to exchange. Social order is built upon activities of relation exchange. Different social orders are distinguished by attributes difference, which is determined by

⁸⁾ Third party norm means to indicate norms such as morality codes, laws, regulations, etc., which are externally imposed as being determined in communitarian decision process or as historical heritage, not determined as contracts making among interests-concerning parties.

institutional composition.

Types of social orders stretch out along the spectrum ranging from primitive anomie to modern civilization. For fundamental propensity of human behavior to break away from anomie of primitive society, third party norms should be set in place. Third party norms cited hereby include heritage of customs, morality, rules, which were built and evolved in the history of society. Regulations, enforced by the government, are also included.

In this research, third party norms are represented in the legal-institutional modules of exchange activities. Three branches of legal-institutional modules are distinguished; morality codes, which naturally emerged and evolved among social constituents, e.g. customs, morality codes, institutions which stipulate on property rights, and prudential regulations which were enforced by the government for efficient sustainment of social order.

Property 3 (Legal-Institutional Modules as Apparatus of Economic Analysis): Due to imperfectness of institution, especially imperfectness of property rights, a legitimate territory is allowed to be set in place for the role operation of legal codes, public administration, and social phenomena as essential elements in economic analysis, off from the operational realm of value exchange of the market.

The concept of relation exchange stretches out the operational territory of exchange from value exchange in the market to ordinary activities of individual's daily life, so that Hayekian concept of spontaneous order becomes rendered more concrete in the newly set institutional dimension. The upshot is that the apparatus of theoretical analysis is set in place and lays basis to provide essential modality of legal-institution to deal with activities of relation exchanges which encompass all the activities of ordinary life of a human being.

Property 3 unfolds that legal, public-administrative, and social phenomena are set in place not as exogenous parts of economic analysis. Morality codes, laws, public administration, and other social phenomena appear as essential elements in economic analysis of relation exchange activities. As the exchange extends the concept to encompass the territory of relation exchanges which are built

upon trust, the institutional factors like morality codes, laws, public administration, and various social phenomena, which used to be regarded as non-essential or exogenous elements, begin to appear as essential elements of theoretical analysis.

2. Legal-Institutional Modality of Relation exchange Order

Analytical ground on which to draw out legal-institutional modality of relation exchange order stems from the logics of Property 3. In this research, the existential modules, *modus vivendi*, of legal-institutional order of relation exchange are distinguished from operational modules, *modus operandi*, when investigating legal-institutional modality. This dual classification approach has been introduced to assess if the decisions of the Constitutional Court in Korea (1988-2003) were friendly with exchange activities. In other words, the approach, which is adopted to incorporate legal-institutional modality of relation exchange activities in this research, doesn't have to be the only standard approach.

When attempting to determine if some individual legal institution is friendly with exchange activities, no institutional methodology to approach to this problem has ever been known to be introduced in the literature. In the subdivision process of academic specialization, researches as such were left aside into blind spot.

Noble contribution of this research may be the location of theoretical clue by the introduction of relation exchange concept, by which we are able to approach this problem.

(A) Existential Modules of Legal Institutions

Existential modules of legal institutions for relation exchange activities have three components: trust, property rights, and public regulatory prudence.

Firstly, relation exchange order is grounded on trust. In a primitive society where property rights were not established yet and where value exchanges in the market didn't appear, such social order should exist as is built upon relation

exchange activities, the setup of which relies upon trusts among individuals, family relatives, and friends. Besides, in a specialized society of modern times where market economy achieved extreme development, the base ground of social order is still built on trust. For instance, if trust or confidence disappears in financial market institutions, financial activities will no longer be effectively operating. Trust certainly remains to hold the position in relation exchange order as more fundamental element than property right institutions.

In this research, trusts are distinguished to be morality codes and trusts in personal relations. Of course, it is not the only way of conceptual classification. Other modules of classification may be considered.

Morality code is a specific module of institution in relation exchange order, which is built on trust relationship. Indeed, it bears the attribute of being grown out from the historical and cultural process of evolution. Hayek called such institutional module and social order extended order, which was shaped in the historical evolution (Hayek 1991).

Personal relationship among individuals includes all the specific personal relationships. They are personal relations among family members, friendship, alumni relations, fraternity built upon solidarity spirits, etc. It is the relation exchange order that grows out from the personal relations.

Secondly, property right is sine qua non, the setup of which should be preceded before value exchanges in the market be drawn out from the society of relation exchanges. Property rights not only bestow the right of ownership to owner, but enforce legal responsibility to social constituents to respect such rights. In this regards, property rights hold legal effectiveness as in the cases, which are classified to be public regulatory prudence, and binding legal enforcement power to be honored. According to the classification scheme of this research, property right may be considered a sort of public regulatory prudence. The reason why property right is separated out is that it builds ground for the functioning of value exchange in the market.

The institutional development of property rights progresses side by side with capitalistic economic development (Demsetz 1967). The establishment of property rights allows the separation of market exchange activities from relation

exchange order. Henceforth, the age of capitalism begins to upsurge.

Here, property rights and contracts are separated and distinguished from broad concept of property rights. The decision to distinguish property rights and contracts followed the English-American common law tradition, while paying regards to the aspects that contracts have grown out from promises among concerning parties. Legal effectiveness of contracts holds binding enforcement power like cases of property rights.

Thirdly, legal institutions of organizational hierarchy, torts, fundamental human rights (FHRs), and other regulatory standards are held distinguished in public regulatory prudence.

Public regulatory prudence sets in place organizational orders to the society which is upheld by relation exchange activities and provides a mould of legal institutions which ensures system stability to the social order. Traffic regulations, taxation codes, accounting standards, and alike, most of public regulations stipulate public regulatory standards.

If the society is constituted by a single person, there is no need for public regulatory prudence. In this regards, public regulatory prudence is no more than problems pertaining to the territory of public choice.

As already discussed, relation exchange order may turn to the order or disorder of a primitive society without the institutional operation of public regulatory prudence. At the worst instance, it could become the disorder of jungle life.

Perhaps, we may argue that the morality codes, which autonomously came off into being in private lives and went progressing through evolutionary process, will keep relation exchange order off from the turnout of worst possibility to fall into the disorder of jungle life. However, in reality, no historical evidence vindicates that morality codes sustain its own viability and function by themselves alone. When morality codes are assisted by institutions of public regulatory prudence, which are enforced by some third parties, either in Hobbesian autocratic polity or in Lockean civil polity, the communitarian social order will function, which is upheld by the institutions of public regulatory prudence which erect on the foundation of morality codes.

Legal institutions of organizational hierarchy indicate institutional modules of

organizational hierarchy, which came into entity in relation exchange order and became operative by the functioning of trust relations. They are legal-institutional modules that are incorporated in the statutes of civil law, commercial law, charter of incorporation, bylaw, and customary codes. Of course, specific type of trust like collegueship as well as generic type of trust, is positioned as undercurrent at the bottom. The relation exchange orders, which are functioning in organizational hierarchy, are put in operation with trust activities as power source which are affected by the attributes of hierarchical institutions, being specific to respective organization.

Torts and regulatory standards are distinguished. Torts indicate judicial disciplinary action, which will be enforced when violation is conducted against legal-institutional modules, which were set to establish trust-based order for the operation of property right system. Illustration of examples may include conducts of violation against statues of property rights and contracts, morality codes, principles of trust and fiduciary duty, bylaws of organizational operation, trust relations in family or among individuals, etc.

In this research, if violation is conducted against property rights, they were classified to be under the title of property rights. Likewise, violations of morality codes, actions against trust filialness, violation of statutes stipulating on organizational operation, cases of violation against trust filialness among family members or individuals were classified to be respectively cases of trust, organizational hierarchy, personal relations.

Other illegal actions, violation of regulation standards were classified under the title of other illegal actions, other regulatory standards. Regulatory standards feature regulation and standards, which are set for the management of public businesses in contrast with private affairs. For instance, environmental regulations, traffic regulations, tax codes, police or military duty, public pensions, public medical services, financial regulations, accounting standards, safety regulations, etc. are the legal institutions that belong to this category.

FHRs are standards of fundamental rights in respective areas for individuals; corporal safeties, freedom of religion, political participation, press and expression, economic activities, hygiene, medicine, etc.

(B) Operational Modules of Legal Institutions

Although the conceptual structure for existential modules *modus vivendi* of legal institutions was proposed in this research, it remains far from perfection.

The imperfectness of existential modules of legal institutions for relation exchanges renders exchange activities becoming exposed to diverse and undetermined institutional conditions. At this juncture, it becomes meaningful to think about how to devise conceptual frameworks for the operational modules *modus operandi* of legal institutions which can represent the diversity of operational attributes of legal institutions, which envisions elements of causal factors which will combine to invigorate exchange activities. In other words, operational modules of legal institutions catch operational attributes of legal institutions for relation exchanges, the attributes of which are the factors that will help invigorate the exchange activities.

Firstly, it is institutional or legal enforceability that will fill the gap between institutional code and effectiveness of rights or between institutional code and effective legal enforcement. If any decisions of the Constitutional Court of Korea (CCK in short) fulfill the role to fill such gaps, such decisions will be classified into this category.

Secondly, it is constitutionality. Constitutionality indicates that decisions of the CCK have introduction effects of new legal effectiveness. It will be investigated if decisions of the CCK have the effect to introduce new elements to existential modules of legal institutions. Same investigation may be conducted to cases of legislations of the legislature, precedents making in supreme court, rulings of the courts at respective stages, and policy makings of the executive branches.

Considering the imperfectness of institutions and historical evolutionary process of institutional development, desirable order of relation exchanges will be approached through the restless process of implanting constitutionality of existential modules of legal institutions.

Thirdly, the third composition factor of operational modules for relation exchange order is accountability. The accountability of each concerned party in legal relations should draw a sharp. It is a fundamental principle that existential

module of legal institutions should comply with.

Since the imperfectness of existential modules for legal institutions is assumed as premise, the operation of legal institutions is complemented by establishing reasonable standards of accountability and responsibility as essential principle among concerned parties in legal rights disputes. The operation of existential modules for legal institutions should be fulfilled in such a way as to honor the principle of accountability and responsibility among concerned parties in legal rights disputes in connection with the operation of property rights institutions, trust- related order management, and enactment and operation of public regulatory standards.

For instance, establishing trust protection as principle in the deliberation steps of the CCK reveals what should be included in the principle of accountability.

Fourthly, the fourth composition factor in the operational module of relation exchange order is the establishment of consistency among legal institutions. New law priority principle and special law priority principle are the legal principles in order to sustain consistency among legal institutions. It is to see to it if new enactments (legislations as well as policy ordinances) or new operation methods of legal institutions (judicial decisions) comply with the sustenance of consistency among legal institutions. It offers particularly meaningful judgment criterion when judicial reviews of the CCK are investigated.

Fifthly, the fifth composition factor of operational module of legal institutions for relation exchange order is to see the effects on free competition. Institutions are bound to follow evolution process. Legal institutions are imperfect by themselves and continue to change through the process of evolution.

It is to see to it if such evolutionary changes of legal institutions tend to enhance the features of free competition in legal institutions.

3. Friendliness of Legal Institutions with Exchange Activities

Two modules of legal institutions for relation exchange order, i.e. existential module *modus Vivendi* and operational module *modus operandi*, when being overlapped, create a two-dimensional conceptual matrix of institutional modules,

as illustrated in Table 1. Conceptual sophistication as such may seem to offer a noble idea in the sense that it lays a foundation by creating a legal-institutional module of exchange activities, which is built upon economics methodology by breaking from the conventional trinity of classification; property rights, contracts, and torts, which are borrowed from jurisprudence.

So far, economics didn't have theoretical foundation upon which to build institutional module of exchange activities by their own methodological logics. Although they acknowledged the importance of the question which institutions are conforming or conflicting with exchange activities (Hayek 1982), they were unable to set a conceptual category with the framework of which to investigate the question. Acemoglu (2004) didn't attempt to determine the friendliness of individual institution but had to be content with comparing the superiority of system, not individual institution, between North and South Korea. For this purpose, two region's incomes per capita were compared for 48 years 1950-98.

Of course, orthodox economics attempt to determine superiority (or inferiority) of institutions by comparing utilitarian welfare measures. Transaction cost approach belongs to this category of approaches. Transaction cost approach, which is often followed when researches are comparing institutions, has a fundamental problem of lack in conceptual clarity (Rhee 2010).

This research identified conceptual determinants, which distinguish institutional modules of exchange activities, by paying heeds to institutional imperfectness and drawing out the concept of relation exchange thereby. It secured a foothold upon which to build theoretical framework with which to determine the friendliness of individual legal institutions with exchange activities.

Conceptual categories of legal-institutional modules in Table 1 were drawn out from two dimensional cross of existential modules and operational modules. Each specific case of institutions should be pigeonholed to one cell or multiple of cells in the matrix in Table 1. For example, rulings of the court (including decisions of the constitutional court), enactments in the legislature, policy ordinances of the executive are on a case-by-case base to be filed to each of cells in the Table 1.

[Table 1] Legal-Institutional Modules of Relation exchange Order

	Enforceability	Constitutionality	Accountability	Consistency	Free Competition
Trust	Confirming trust as sources of law	Identifying new fields where trust being conceived as source of law	Confirming the principle of accountability in relations as formality for source of law	Confirming the principle of institutional consistency in trust relations as formality for source of law	Applying the principle of free competition to trust relations and confirming it as formality for source of law
Morality Codes	Confirming morality codes as sources of law	Identifying new fields where morality codes being conceived as source of law	Confirming the principle of accountability in morality codes operation as formality for source of law	Confirming the principle of institutional consistency as formality for source of law while taking morality codes as source of law	Applying the principle of free competition to morality codes operation and confirming it as formality for source of law
Personal Relations	Conventional behaviors, which sustain personal relations, being confirmed as sources of law	Identifying new fields where personal relations being conceived as source of law	Confirming the principle of accountability in personal relations management as formality for source of law	Confirming the principle of institutional consistency, as being applied to personal relations management, as formality for source of law	Confirming the principle of free competition, as being applied to personal relations management, as formality for source of law
Organizational Hierarchy	Confirming the sustanment and operation of organizational Hierarchy as formality for source of law	Identifying new fields where personal relations being conceived as source of law	Confirming the principle of accountability in the management of organizational hierarchy as formality for source of law	Confirming the principle of institutional consistency, as being applied to the management of organizational hierarchy, as formality for source of law	Confirming the principle of free competition, as being applied to the management of organizational hierarchy, as formality for source of law
Property Rights	Filling the gap between property right as	Identifying the fields, categories, and cases	Confirming the principle of accountability as	Confirming the principle of institutional consistency,	Confirming the principle of free competition, as

	institution and effective ownership with judicial enforcement	where property rights are newly established	formality for source of law to enforcement of property rights	as being applied to the exercise of property rights, as formality for source of law	being applied to the establishment of property rights, as formality for source of law
Contracts	Filling the gap between contract as institution and effectiveness of contract with judicial enforcement	Identifying the fields, categories, and cases where contracts being upheld as formality for source of law	Enforcing the principle of accountability, while being applied to contracting activities, as formality for source of law	Enforcing the principle of consistency in the legal and institutional operation of contracts, as formality for source of law	Confirming the principle of free competition, as being applied to the making and operation of contracts, as formality for source of law
FHRs 1)	Filling the gap between FHRs as institution and effectiveness of human rights with judicial enforcement	Identifying the fields, categories, and cases where FHRs being upheld as source of law	Enforcing the principle of accountability, while being applied to the exercise of FHRs, as formality for source of law	Enforcing the principle of consistency in the legal and institutional structure related to the FHRs	Confirming the principle of free competition, as being applied to legal implementation of the FHRs, as formality for source of law
Torts	Filling the gap between torts as institution/standards and institutional effectiveness with judicial enforcements	Identifying the fields, categories, and cases where torts as institution/standards being upheld as source of law	Enforcing the principle of accountability, while being applied to the implementation of torts as institution/standards, as formality for source of law	Enforcing the principle of consistency in the legal and institutional structure related to torts	Confirming the principle of free competition, as being applied to legal implementation of torts as institution/standards, as formality for source of law
Other Regulatory Standards	Filling the gap between other regulatory standards as institution and effectiveness of standards as such with judicial enforcements	Identifying the fields, categories, and cases where other regulatory standards as institution being upheld as source of law	Enforcing the principle of accountability, while being applied to the implementation of other regulatory standards as institution, as formality for source of law	Enforcing the legal/institutional consistency among other regulatory standards	Confirming the principle of free competition, as being applied to the operation of other regulatory standards, as formality for source of law

Table 1 explains conceptual categories of each cell, which was made out of two dimensional cross of existential modules and operative modules of legal institutions.

Individual cases of institutional introduction are classified according to conceptual categories of the table so that the location of each case into appropriate cell is determined. At each case of institutional implementation, it was determined if the institutional change is proactive or retroactive when it is judged according to the concept of conceptual categories of located cells. Assessments of whether institutional changes are proactive or retroactive cannot but rely on qualitative judgment.

For instance, a case assigned to modules trust and enforceability will be assessed according as the case makes proactive or retroactive effects on the evolutionary steps to improve legal enforceability and help recognize trust as source of legal power. Another illustration of cases assigned to modules morality codes and accountability is that the case will be assessed according as individual case of institutional implementation makes proactive or retroactive effects on the evolutionary steps to improve accountability and help recognize morality codes as source of legal power.

Such modular classification approach of institutions seems to logically match path dependence of institutional changes. If exact transaction costs are able to be calculated in each of institutions, path dependence of institutional change will not hold good.

If individual case of institutional introduction is assessed proactive according to conceptual categories of the assigned cell, such introduction of institution is judged to have improved the friendliness of legal institutions with exchange activities. For example, suppose the question is if enactments in the legislature in a particular year, policy implementations of the executive for a specific period, and rulings of the courts reveal friendliness with exchange activities. Then, it will be determined according as institutional changes recorded in Table 1 according to conceptual categories of modules are assessed proactive or retroactive. In a nutshell, qualitative comparisons of friendliness of the decisions among different branches of the government become possible; enactments in the

legislature for a specific period, policy implements of the executive, and decisions of the constitutional court.

IV. Friendliness of CCK Decisions (1988–2003) with Exchange Activities

This research was conducted on 123 cases of decisions of the CCK, which were filed for trial during the period 1988–2003. Among them, the cases, the original claims of which brought to deliberation, were selected. Cases of jurisdiction disputes among branches of the government were excluded. Finally, 29 cases that are well related to exchange activities were selected for analytical investigation⁹⁾.

29 cases of CCK decisions were classified according to the modules of legal institutions in Table 1 and are presented in Table 2.

[Table 2] Friendliness of CCK Decisions (1988–2003) with Exchange Activities

	Enforce-ability	Constitution-ality	Account-ability	Consis-tency	Free Competition
Trust	24				
Morality Codes	15				
Personal Relations	16				
Organizational Hierarchy	29				
Property Rights	7, 9, 23	17	8, (19), (20)	12	18
Contracts			26		21
Fundamental Human Rights	11, 14, 22	1, 5, 6	10		
Other Torts				13	
Other Regulatory Standards		2, 3, 4		25	(27), 28

Note: 1) Numbers in the table indicate serial numbers of 29 cases listed in Table A1.

2) Numbers in the parentheses in the table indicate that the cases were assessed retroactive according to the categorical concept of the assigned cell. Numbers without parentheses indicate proactive assessment.

⁹⁾ Precedents' id numbers of 29 cases are listed in the table A1 in the appendix.

Reading of 29 cases in Table 2 and cases distribution there reveals that more of cases are concentrated in the modules of Property Rights, FHRs, Other Regulatory Standards. Cases are also distributed to Trust, Morality Codes, Personal Relations, Organizational Hierarchy, and Other Torts. However, they are merely fewer.

The reason for such turnout seems that the cases under investigation in this research are decision precedents of the CCK. It may be guesstimated that if cases were precedents of lower court rulings, more cases of disputes would be found in latter modules.

Outcome of distribution in Table 2 discloses that decisions of the CCK were retroactive to exchange activities only in three cases (19, 20, 27). In other 26 cases, CCK decisions were proactive to exchange activities.

In three retroactive cases, decisions of the CCK didn't make negative effects on exchange activities by themselves. Negative effects on exchange activities had already been extant there since the moment of policy implementations, administrative ordinances or enactments in the legislature. Decisions of the CCK were upholding already extant negative measures and didn't create any additional negative effects. Exchange activities are not relieved by decisions of the CCK, nor are repressed further.

In this regard, judicial reviews tend to influence positive effects on exchange activities and are not bound to make negative effects¹⁰⁾. The rule of law turns out to be friendly with exchange activities¹¹⁾.

¹⁰⁾ Why seemingly natural conclusion sounds bewildering? The reason seems likely that we are not familiar with such logical exercise because institutional dimension is lacking in the analytical structure of orthodox economics. Even new institutional economics approach fails to add institutional dimension. They adhere to the analytical structure of orthodox economics and attempt to interpret institutional phenomena accordingly into the structure. Transaction cost approach is a typical example (Rhee 2010).

¹¹⁾ t-test was conducted to 29 CCK decisions to determine if CCK decisions make positive (or negative) effects on exchange activities. If CCK decisions were classified proactive, value 1 is given, whereas value 0 is given if CCK decision was classified retroactive. The reason why 0 value, not -1, is given to retroactive CCK decisions is that negative effects of, say, administrative ordinance of the executive was reaffirmed but would not be rendered worse by decisions in the court. Outcome of test was the turnout of positive results to exchange activities with 99% level of significance.

V. Concluding Remarks

Is the rule of law friendly with exchange activities? Orthodox economics are not prepared with appropriate theoretical foundation upon which to answer the question. The reason is that the concept of institution does not exist as theoretical dimension in the theoretical structure of orthodox economics. New institutional economics approach, which is built on transaction cost analysis, is no exception. They stand put in traditional position of analytical structure in orthodox economics and merely attempt to interpret the concept of institutions by means of traditional analytical tools. Institutional dimension is not conceived as independent axis of analysis.

In this research, attention is paid on the imperfectness of institutions. Relation exchanges, which arose from imperfectness of institutions, enable the objects of economic analysis to stretch out from value exchanges in the market to the territory of relation exchanges. By recognizing value exchanges in the market as special cases of relation exchange when property rights are perfectly secured, all daily activities of individuals became part of relation exchanges and became objects of economic analysis. Hence, institutional dimension became put in place as independent axis of economic analysis.

The location of institutional dimension as independent axis in economic analysis indicates that it becomes possible to locate relation exchange order as social order. For instance, it becomes possible to analytically draw out the role of third party, e.g. government, from Hobbesian social contracts, which performs to secure the stability of social order.

The building of theoretical base as such rendered it possible to recognize institutional phenomena like morality codes, law, public administration, and other social norms, which upholds stable operation of social order, in the analytical structure of relation exchanges. The ability to recognize institutions like morality codes, law, public administration, etc. in analytical structure of relation exchange means to indicate that analytical foundation has been built to determine if such legal institutions are performing friendly with exchange

activities.

Analytical structure to determine if decisions of the CCK (1988-2003) were friendly with exchange activities was built.

Introduction of two dimensional concepts, i.e. existential modules *modus vivendi* and operational modules *modus operandi* of legal institutions, and through their intercross, rendered it possible to construct conceptual categories for legal-institutional modules of relation exchange order. Nine module concepts were distinguished in existential modules of legal institutions, such as trust, property rights, regulatory standards, etc. Five module concepts were distinguished in operational modules of legal institutions, such as enforceability, accountability, etc. Matrix intercross of two different modules creates 45 module composition elements.

Each decision of the CCK was assigned to one of 45 conceptual categories and pigeonholed as such. Proactivity or retroactivity of each decision was determined according to conceptual categories of the cell in the module matrix.

Only three cases out of 29 decisions of the CCK (1988-2003) were classified retroactive. The rest 26 cases were assessed proactive to exchange activities. The outcome indicates the friendliness of CCK decisions with exchange activities. Three CCK decisions, which were assessed retroactive, didn't mean to have made additional negative action to repress exchange activities. It indicates merely that the decisions were unable to correct already extant retroactive legal institutions.

In a nutshell, the outcome of research seems to establish the proposition 'the rule of law cannot but be friendly with exchange activities.' How does the proposition, which is seemingly evident, sound bewildering? The absence of institutional dimension as conceptual axis in analytical structure of orthodox economics seems to be the essential reason. Due to defects in analytical structure, such important institutional questions remained hidden to our intellectual recognition.

[Table A1] Case Numbers of the CCK and Serial Numbers

1: d2000k009	11: d90k023	21: d99m143
2: d2000m091a	12: d90b001	22: d98k016
3: d2000m091b	13: d91k004	23: d98k013
4: d2000m092	14: d91m111	24: d98k012
5: d2000m546	15: d99m481	25: d98k008
6: d2000s471	16: d98m168	26: d98k006
7: d89m031	17: d94b037	27: d98k001
8: d89m204	18: d99k018	28: d96k018
9: d89m214	19: d99m365	29: d96b033
10: d90b022	20: d99m289	

REFERENCES

- Rhee, Sung Sup (2004), "Judicial Review and Market Institutions: Case of Korea," presented at Annual Meeting of Southern Economic Association at Baltimore in March 2004 and also presented at Brown Bag Seminar at Buchanan House, George Mason University, in April 2004.
- _____ (2010), "Market Exchange, Relational exchange, and Evolution of Market Institution," presented at 2010 KIEA International Conference on Institutions and National Competitiveness II, convened in August 10-11, 2010 in Seoul, Korea.
- Acemoglu, Daron, Simon Johnson, James Robinson (2004), "Institutions as the Fundamental Cause of Long-Run Growth," in *Handbook of Economic Growth*, edited by Philippe Aghion and Steve Dulauf, North Holland, 2005.
- Chandler, D. Alfred (1992), "Organizational Capabilities and the Economic History of the Industrial Enterprise," *Journal of Economic Perspective*, Vol. 6, No. 3, 79-100
- Demsetz, Harold (1967), "Toward a Theory of Property Rights," *American Economic Review*, LVII (2), 347-59.
- Dworkin, Ronald (1986), *Law's Empire*, Harvard University Press.
- Eggertsson, Thrainn (2005), *Imperfect Institutions: Possibilities and Limits of Reform*, University of Michigan Press.
- Fukuyama, Francis (1995), *Trust: The Social Virtues and the Creation of Prosperity*, Free Press.
- Hart, O.D. (1987), "Incomplete Contracts," In J. Eatwell, M. Milgate, and P. Newman, eds., *The New Palgrave: A Dictionary of Economics*, 2:752-59, London: Macmillan.
- Hayek, F. A. (1991), *The Fatal Conceit: The Errors of Socialism*, edited by W.W. Bartley III, The University of Chicago Presss.
- _____ (1982), *Law, Legislation and Liberty*, Routledge & Kegan Paul.
- John Locke (1690), "Two Treatise of Government", printed in *Two Treatise of Government and A Letter Concerning Tolerance*, edited in Rethinking the Western Tradition Series with Ian Shapiro as editor in 2003.
- Douglass C. North (1990), *Institutions, Institutional Change and Economic*

Performance, Cambridge University Press.

Douglass C. North, John J. Wallis, Barry R. Weingast (2009), *Violence and Social Orders: A Conceptual Framework for Interpreting Recorded Human History*. Cambridge University Press.

Robert E. Scott and Jody S. Kraus (2002), *Contract Law and Theory*, Revised Third Edition, LexisNexis.

Oliver E. Williamson (1985), *The Economic Institutions of Capitalism*, The Free Press.

Thomas Hobbes (1651), *Leviathan*, reprinted in Penguin Classics in 1985.

국문초록

법의 지배는 교환활동에 친화적인가?

이 성 섭
(송실대학교 글로벌통상학과)

제도는 원초적으로 불완전하다. 이것은 인간인지능력의 한계와 결합하여 인간생활에서 극복할 수 없는 제약조건이다. 사람들은 이 상황을 관계교환으로 맞서왔다. 시장의 가치교환은 관계교환의 특수한 상황(부분집합)이다. 즉 사람들은 관계교환질서 속에서 살고 있다. 이것은 도덕 및 법규범으로 이 관계교환질서를 잘 관리하면 교환활동을 왕성하게 하는 관계교환질서를 만들어낼 수 있다는 것을 의미한다. 이 현상을 확인하기 위해서 한국의 헌법재판소 경제관련 판례 29건을 조사하였다. 2개의 법 작용양식(존재양식 existential modules, 작동양식 operational modules)을 구분하여 45개의 교차적 법 운용양식 개념을 분류하였다. 각 판례가 45개 각 개념에 속하는 분류에 귀속시켜서 교환활동에 긍정적이었는지 부정적이었는지를 평가하였다. 3건의 부정적 경우를 제외하고 나머지 모두 교환활동에 긍정적 내용의 판례였다는 결과를 얻었다. 이것은 법치 그 자체가 교환활동에 친화적이라는 것을 말한다. 즉 관계교환질서가 법치에 의해서 교환활동에 친화적으로 운용되고 있음을 확인한다.

주제어(Key words): 제도의 불완전성, 관계교환, 가치교환, 법치, 교환활동 친화적

【2012. 11. 15. 접수】 【2012. 11. 26. 수정】 【2012. 11. 27. 게재확정】