



# Large courts, small justice! ☆

## The inefficiency and the optimal structure of the Italian justice sector



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### ABSTRACT

An important problem in the public sector, given the lack of output prices and exit decisions to sanction inefficient units, is finding the optimal industry structure. We apply a novel approach to Italian courts of justice, a typical example of a small sector in the public domain but with important effects on economic agents' behavior, firm size, FDI, and on the overall economy. The suggested approach enables us to break down the aggregate court inefficiency into different sources and to investigate the optimal structure of the justice sector. Results show that technical inefficiency (lack of best practice) accounts for more than one third (38%) of total inefficiency, while size inefficiency (courts that are too big) is about 22–25%. The remaining inefficiency is represented by a sub-optimal allocation of inputs (30–40%). If reallocation is confined to macroregional or regional borders, then technical and size inefficiencies increase in relative terms compared to reallocation inefficiency. We suggest that, together with reallocating inputs by merging smaller courts, a complementary set of policy interventions would be to adopt best practices and split larger courts.

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## 1. Introduction

The recent financial crisis and the ensuing sovereign debt crisis have produced a growing awareness of the need for structural reforms in order to increase the public service efficiency and sustain higher economic prosperity. One of these reforms concerns the structure of the judicial system and its effects on the enforcement of contracts. With reduced public funds available, an underfunded and unreformed court system could weaken the economy and the access to justice [15]. Some radical proposals in the UK suggest that courts might even be privatized [21].

Although small when compared to the whole economy, the judicial system and the rule of law have a very significant impact on economic behavior, investment choices and economic development [1]. Economic agents (households and firms) might exploit delays in justice delivery to strategically postpone their contractual obligations to other parties. For example, debtors might choose opportunistically to be sued by their creditors hoping to obtain a substantial delay of the repayment deadline (see, e.g., [23]). Court inefficiencies have also a detrimental impact on firm size [12]. Furthermore, the justice sector is a typical example of a

critical sector of the economy where the market system cannot work properly given the absence of a functioning output price mechanism. Lack of output price information means that it is difficult for agents to sanction inefficient units.<sup>1</sup>

Therefore, it becomes particularly useful to envisage a method for measuring inefficiency and potential optimal structures of the sector in order to set effective policies aimed at improving its overall efficiency. In this paper, we investigate the efficiency of Italian courts of justice, by proposing a new general method for estimating the optimal structure of public sector industries. The efficiency of the justice sector has received relatively limited attention in the literature [35].<sup>2</sup> More commonly we find partial performance measures, such as trial length and the number of cases defined per judge (see, e.g., [7]). Efficiency analysis, however, allows performance to be measured by taking into account all the resources used and all the outcomes produced.

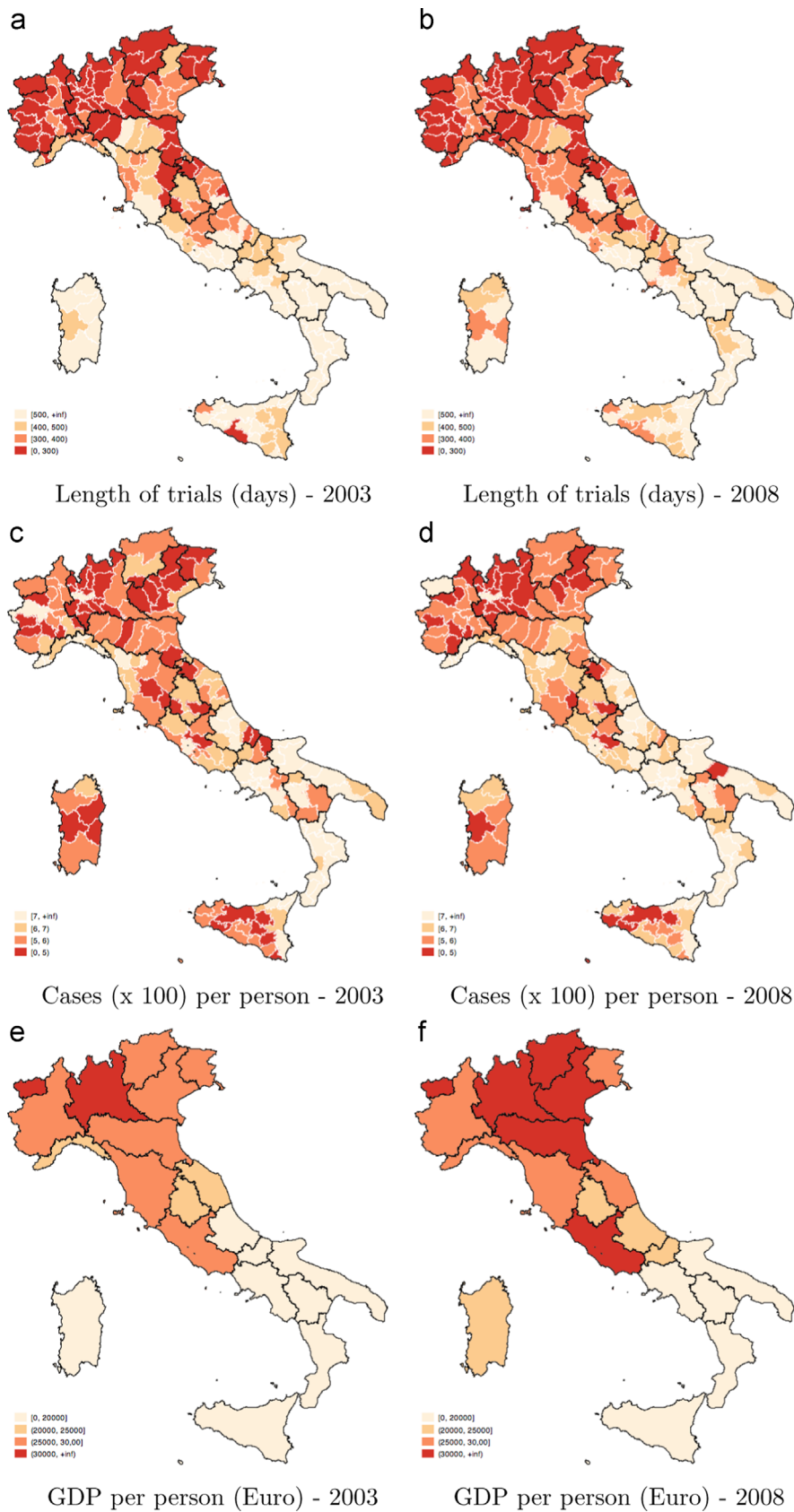
By international standards, the Italian judicial system is quite inefficient. According to the World Bank's *Doing Business 2012*, in

<sup>1</sup> In addition, in Italy, like in many other countries, cases are assigned to the local court district and thus citizens cannot “choose with their feet”, that is decide to which court to bring their case to.

<sup>2</sup> The reason for the paucity of papers investigating judicial system efficiency might be that data at the court level are difficult to obtain. In this paper, we use a rich dataset describing all the Italian courts of justice (165 observations) from 2003 to 2008.

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**Fig. 1.** Supply, demand of justice, and economic activity.

terms of enforcing contracts, Italy ranks 158th out of the 183 countries covered in the survey (compare this, for example, to Germany (8th), Belgium (20th), UK (21st), and Spain (54th)). In

2011, the average citizen had to wait about 900 days to obtain a trial with judgment [39]. In addition, while in Europe the average time for litigious civil and commercial cases was 282 days (median

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