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The perils and benefits of non-traditional legislation

A Paper for the Progress Foundation, Switzerland

By Graham Mather

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What was government has become governance. Where once elected politicians passed legislation and signed treaties to determine our futures, today un-elected experts make rules through soft law.

To prove this proposition, let me turn to the financial crisis and the way in which it hit Europe.

First into action to provide liquidity was the European Central Bank headed by its President, Jean-Claude Trichet. Although he has been named Policy Maker of the Year on more than one occasion he has never been a minister, never a politician, never elected. But this gifted *enarque* and his Central Bank colleagues, in their provision of liquidity, quantitative easing, bank guaranteeing and money printing determined, governed the response to the crisis.

Once the authorities had their breath back they looked for solutions in the longer term. They turned to Jacques de Larosière, another supertalented French banker and public servant. A former head of the IMF and EBRD, again he has never sought election to a parliament and was appointed by decision of the European Commission. Yet his report was and is the foundation of Europe's response to the crisis.

As Europe and de Larosière turned to align their measures with those of the United States, the spotlight moves to the G20. Another soft law creation, it did not exist 10 years ago when the G7 and G8 were the main focus of global financial discussion. It is self-appointed, has no charter, and no treaty determines its rules or its membership. Yet it is the lead body for the raft of measures which are being taken around the world to emerge from the financial crisis. The European Commission will show you a table against which it checks off its compliance with the G20 norms.

Swing back again to the proximate causes of the financial crisis. How do we decide whether banks are or are not properly capitalised? Again, by soft law. The Basel Accords must assume their responsibility. Whether Basel I, II or III the capital adequacy rules are decided informally and their status is as recommendations. The Basel Committee, which now includes the G20 countries, therefore recommends capital adequacy measures without a treaty or constitutional framework; only later are the recommendations turned into national or European laws.

When the crisis moved from banks in the market to the risk of sovereign default, the foundation instrument turned out to be another piece of, this time European soft law – the Stability and Growth Pact of the European Union. It has never been fully constitutionalised and comprises a Council Resolution, Two Council Regulations and a Code of Conduct. This uneasy mixture makes it in academic terms a hybrid between soft law and hard law, or more bluntly "a stability pact ridden with holes". (Habermas 2010).

When Europe acted to bail out Greece it did not do so under Treaty or legislative powers – rather it created a special Intercreditor Agreement between 15 eurozone member states at short notice on 8 May of that fateful weekend. The soft nature of the transaction is demonstrated by the fact that Slovakia's Parliament on 18 August refused by 69 votes to 2 to ratify the agreement.

These were crisis measures. But in the daily running of the European Union also, much policy in labour markets, the environment and elsewhere takes place through the Open Method of Co-ordination. The OMC is a series of soft law techniques of discussion, co-operation, benchmarking and peer-review. The procedures are unmentioned even in the Lisbon Treaty.

My purpose in this lecture is not to suggest that hard law is good and soft law bad. It is rather to sketch the extent of soft law, to look at its causes and rationale, to assess its merits and problems and then to draw some conclusions for future public policy arising from it.

How can we define soft law for our purposes? Once upon a time it might have been thought of as a series of 'gentlemen's agreements' but both the term and language has a rather dated feel. (Williamson, 2003).

Linda Senden has provided the definition which I found most persuasive; that soft law is formed by “rules of conduct that are laid down in instruments which have not been attributed a legally-binding force as such, but nevertheless may have certain indirect legal effects that are carried out and may produce practical effects”. (Senden, 2005).

Or as Ulrika Mörth has noted “in systems of government the law is hard whereas it is soft in systems of governance. The crucial difference between these two types of legal norms is that soft law lacks the possibility of legal sanctions”.

The fact that soft law lacks legal sanctions does not mean that it does not attempt to impose sanctions by a range of techniques. They are enforceable or sanctionable at various different levels by means, not of law, but of some form of perceived international responsibility. These systems lack legal rights or obligations, they also lack procedural safeguards and they often lack transparency: and these are serious weaknesses.

In the context of the OECD’s initiative on so called harmful tax practices Allison Christians has said that the category of soft law “seems to offer a third way between the potentially uncomfortable position of describing the OECD guidance as ‘law’ and therefore implying states must comply with it, and the potentially unrealistic position of describing it as not law at all, despite evidence that countries do in fact comply with it, often against their self interest or will (or both)”. (Christians, 2007).

The Stability and Growth Pact provides a good example. We immediately see its soft law origins: a deficit above 3% is not excessive if the excess over 3% is only “exceptional and temporary” and the (government deficit) ratio remains “close to the reference value”. As has been noted, there has been considerable manoeuvrability within those limits.

Procedurally it can take three years from the beginning of an excessive deficit before sanctions are applied to an EU members state. These sanctions have never had much credibility as the first is a non interest bearing deposit. Furthermore when the Stability and Growth Pact threatened to affect large countries France and Germany procured its redesign in 2005 to make it easier to elongate the procedures and avoid sanctions.

Academic commentators noted then that “it is true that this system has failed to work as originally hoped. In the current conjuncture several states, including some of the larger ones, have breached the excessive deficit limits for some time. The soft law system could

not prevent this development and the Union's inability to deploy the hard law sanctions has forced the EU to reconsider the original design". (Trubek, Cottrell and Nance, 2005). Since those words were written in 2005 the further stresses on the SGP have generated another search for a more robust system, in the Van Rompuy task force. The hybridity of hard and soft law has not proved effective.

Putting it bluntly, soft law leads to soft compliance. (Cini, 2000). Soft law is not legally binding in itself and indeed has often been deployed because countries are unable or unwilling to secure parliamentary, constitutional or treaty approval for a course of action. But if implementation rests on the goodwill of those agreeing to a non-binding measure not only is this an unstable foundation. It can suffer from a number of other serious defects.

In soft law processes:

a) Established legislative procedures are abrogated;
b) Parliaments tend to be bypassed;
c) Its content is often vague and non justifiable;
d) It may be inconsistent with existing legislation;
e) It may be inaccessible and opaque with little scope for public engagement;
f) It may lack for all these reasons a proper scrutiny and review; and
g) It may allow bureaucrats a dominant role in the creation of policy (Cini, 2000)

Another phenomenon which is detectable in the use of soft law techniques is that the interests of small countries tend to be pushed to one side. As Konrad Hummler has said, soft law is the law of the powerful. The complex design of the European Union was intended to reduce this risk, although as unanimity has given way to qualified majority voting, the unease of small countries such as the Benelux with what they see as a 'directory' of large member states (Germany, France and sometimes Britain) has increased. When initiatives ultimately derive from, for example, the G20, the de Larosière report or the Basel Accords it becomes even less likely that the voice of a particular small country, or small countries as a group, will be a significant influence in European policy making. In the same way the OECD's soft laws on tax have clearly been part of an assault on lower tax smaller coutnries by higher tax larger countries.

Sometimes it can be difficult to tell whether a shift to soft law is part of a genuine modernisation of policy approaches or simply an attempt to bypass obstacles created by the traditional methods of lawmaking. New governance, post-regulatory policymaking and new proceduralism can encompass devolution, public private partnerships, new types of regulation and incentives, networks, co-ordinated data collection and dissemination, benchmarking and new forms of citizen engagement (Trubek, 2006).

The EU's Open Method of Co-ordination may be an example of modernising developments designed to promote the Lisbon market opening techniques, in areas where traditional legislation was politically contentious or had become bogged down.

Its typical modus operandi has been the promulgation of inspirational objectives, targets or goals and agreement by a group or sub-group of member states to follow that line of policy direction. It began in the European Employment Strategy, a set of non-binding guidelines designed to govern the reform of national laws, policies and institutions in order to make them more employment-friendly. It has reports, indicators, benchmarking, peer review and exchange of best practice, and overall seems to have benign effects.

Attempts were made to include a definition of the Open Method of Co-ordination in the Lisbon Treaty but these foundered largely because of antagonism to the perceived inter-governmentalism of this approach by some of the left and more federally minded in the European Convention debates. This is unfortunate, because it left the Open Method of Co-ordination vague and ill-defined, and this form of soft law absent from the main constitutional document of the European Union for the foreseeable future.

This lack of constitutionalism has been very noticeable in the activities against so-called harmful tax competition launched by the OECD. The work of the OECD's Fiscal Affairs Committee, a group of revenue officials, is opaque; it has not hesitated to use techniques of blacklisting and grey listing which exert disproportionate pressure on small counties to raise their taxation levels and remove incentives which might attract large country tax payers to their shores; at times the work has almost seemed to be a personal crusade by one prominent official in the OECD; and the very limited checks and balances within the OECD structure such as its Business and Industry Advisory Committee have seemed entirely ineffectual.

The enthusiastic officials within the OECD have seized upon other new soft law techniques, including Global Forums, to extend this work to non-member counties. As a former

ambassador to the OECD explained “the outcomes of the Global Forum meetings are reported to committees that decide whether any follow up is required. Flexibility, informality and inclusiveness are great assets to the Global Forums. Global forums provide an alternative venue for systematic engagement with non-members. They promote multi-disciplinary and horizontal approaches beyond the scope of any single committee and foster partnerships with other inter-governmental organisations. They are an important recognition that it is possible to bring together those who share a common interest without traditional membership”. (Buorgon, 2009).

This enthusiastic account is rather worrying. Not only does the OECD operate in a way which is not favourable to the smaller countries in its own membership; but it sets up systems to deal with third countries which are characterised by ‘flexibility and informality’ and entirely lack oversight, scrutiny, traditional legislative legitimacy or the checks and balances associated with the creation of treaties and hard law.

The economic crisis has tended to shift the gaze of policy makers from corporate social responsibility. It and other attempts to control the behaviour of corporations have been characterised by the use of soft law; they stemmed from the uncertainties of capitalism in the 1970s and 1980s. Repeated attempts from the left to establish a United Nations code for multinational corporations had failed so, as academic commentators noted, “Therefore Corporate Partnerships were seen as a promising new way to attract political and financial support for the UN, after more than a decade of heavy criticism from important sectors of business, conservative foundations and think tanks, particularly in the US”. (Baccaro and Mele, 2009).

The UN Global Compact is an international initiative to bring together companies, labour, civil society and UN agencies in support of what have been termed universal, social and environmental principles. It is interesting that the enforcement mechanism of the compact is through organised groups of influential investors.
These investor advocacy organisations show signs of the same lack of accountability, preparedness to set their own agendas and use of quasi-sanctions against companies which fail to comply with the codes they have promulgated.

Soft law can tend to elevate the role of NGOs, which have their own problems of lack of accountability, self selected mandates and absence of checks and balances. As Tony Blair said of NGOs in his memoirs: “As it’s all about impact, they shout louder and louder to get heard. Balance is not in the vocabulary. It is all ‘outrage, ‘betrayal’, ‘crisis’.

They also have their own tightly defined dogma and conventional wisdom which, if you challenge them, they defend fiercely - not usually on the merits, but by abusing your motives for challenging them”. (Blair, 2010).

Soft law systems frequently interact and cross refer. International bodies issue and promote general declarations of good conduct, and then involve public and private actors in implementation. Some companies sign up to these initiatives in the hope of a quiet life and reputational boost. Others see in such developments opportunities to exclude smaller competitors. Wiser corporations prefer legal certainty, due process and the traditional enactment of legislative and regulatory measures.

There is a public choice problem, also. Research suggests “that international organisations choose network management solutions not so much due to their technical superiority vis a vis other forms of regulation, but rather as a form of domain appropriation: instruments like global corporate codes impose minimal requirements on the constituents, and thus avoid the most pressing problems of political acceptability, but at the same time allow international organisations to assert their role in the policy areas in question”. (Baccaro and Mele 2009). Or as Tony Blair puts it “the trouble with some of them is that while they are treated by the media as concerned citizens, which of course they are, they are also organisations, raising money, marketing themselves and competing with other NGOs in a similar field”. (Blair 2010).

Again this pattern must give rise to concern. A Faustian pact between the largest global corporations and international bureaucracies and NGOs concerned about their financial position and place in the sun may not be the optimal design for the development of public policy or indeed corporate behaviour, market entry, competition, choice or consumer welfare.

The European Union is a community of law. Directives are binding but allow member states a certain leeway as to detailed implementation. Regulations are directly applicable. Recommendations from time to time issued by the European Commission or Opinions and Communications are ‘constitutional’ and mentioned in the Treaty. It is clearly in Europe’s interest to continue to be a community of law.

In this way the de Larosière recommendations will eventually be fully legalised under the Union’s processes; the Basel III Guidelines will be transformed into a Capital Requirements Directive and the interactions in the G20 on, for example, bankers pay will ultimately materialise as binding community law in the usual way. This is as it should be.

Indeed there are interesting, contemporary examples where the EU institutions have used hard law to 'legalise' what could otherwise have been a rather chaotic and undignified scramble as member states fought to shore up their banking and financial sectors. The Directorate General for Competition deployed a shrewd hand in subjecting bailouts and guarantees to the EU's state aid rules. First the Commission captured what was going on and tabulated it; it went through the motions of considering and approving the state aid concerned even if, as in the case of Ireland, the member state had acted first and told the Commission later.

As a result the Commission is now in a relatively strong position to police an exit strategy. It placed a useful framework around the bank rescues, acted against member states planning to favour national champions in the process and established a system by which the eventual wind-down of the guarantees can be conducted transparently and subject to the institutions' supervision.

This transition from soft law to hard law compares favourably with the attempts to create hybrid instruments as in the Stability and Growth Pact. In the latter case, the concepts of soft and hard law are jumbled together with predictably unsatisfactory results. In the application of state aid rules to bank rescues, soft law developments have been subjected to a pre-existing hard law framework with much more satisfactory outcomes.

In the area of taxation, by comparison, the European picture looks much less satisfactory. Because the Treaty continues effectively to require unanimity for taxation policy changes the Commission has long been frustrated by its inability to move towards, for example, a common consolidated corporate tax base. The plan remains on the back burner and yet another attempot to revive it is expected in 2011.

But in the case of tax incentive schemes developed by member states to boost enterprise and growth, the Commission succeeded, in a more activist era, in establishing a soft law Code of Conduct on Business Taxation which has stamped out many job creating pro-competitive tax approaches. It has performed a stately *pas de deux* with the OECD's activist initiatives. It has used the same techniques of naming and shaming, peer review, enumeration of a list of practices deemed to be harmful and arm-twisting pressure to secure the aims of standstill against further pro business tax incentives and roll back of existing initiatives. In some cases fairly crude tradeoffs have been established by which countries have agreed to roll back elements of their own tax regime only if favourable elements of other countries regimes are also attacked.

The Code of Conduct Group of ministers and officials who have run these policies has no treaty legitimacy, is not subject to European Parliament scrutiny or control, meets in private, produces only the most vague and general accounts of its work and generally scores badly against all tests of modern good government or governance.

This absence from the treaty of such important areas of soft law is of particular concern because it leaves it vague as to how they should be used and policed. "The (Lisbon) treaty does not even mention such frequently soft used instruments as resolutions, conclusions, declarations, codes of conduct, codes of practice and guidelines". (McLure 2007).

The prevalence of soft law makes it important that these omissions are corrected. The EU has developed a world class approach to better regulation and impact assessment: it is well placed to take a leadership position to clarify and categorise the way in which soft law should be used. It is important that this is done. At every level from the G20 through the Stability and Growth Pact, through the open method of co-ordination and in groupings within the EU and with third countries hard law is being avoided.

To reform these systems effectively policy makers will need to stand back and look at the pros and cons of soft law techniques. Is soft law transitional or an independent form of legislation and regulation? Many of our examples so far in this discussion have shown a preparedness to take soft law initiatives and legalise them into hard law.

Clearly the spread of soft law is testimony to its attractions. We should not criticise policy makers for the use of techniques like the development of consensus either within a state, within the European Union or in a broader global grouping. Aspirational policy making which looks towards ambitious targets can be effective, both politically – in raising expectations – and operationally in providing focus for officials. Benchmarking is a profoundly useful tool. Modern IT allows us to make much greater use of comparative data than was historically the case.

Nation states which subject themselves to peer review do so consciously. It is indicative that whilst all EU member states are prepared to allow certain aspects of their tax policy to be scrutinised and criticised in this way, it is taking much longer to make progress on broader economic and fiscal policy. The ambition of the European Central Bank to go beyond an excess deficit procedure to an "excess vulnerability procedure," on a range of economic indicators, will test this preparedness.

Blacklists and grey lists are not attractive. The Stability and Growth Pact has found it very hard to shame countries into action on fiscal deficits. There is a limit to the degree to which members of a club can be sanctioned. It is notable that most current proposals attempt to strengthen sanctions by automaticity, that is to say by removing the likelihood that fellow ministers will give a country the benefit of the doubt and seek to avoid the moment of penalty in opposition. The automatic approach seeks to impose the penalty first and allow member state intervention only thereafter. Does such a system have a feel of being likely to work? Or does it conceal a deeper problem, perhaps indeed the absence of an optimal currency area.

These difficulties illuminate the downside of soft law techniques. The most obvious for lawyers is probably that soft law raises illusory expectations of compliance. Soft law blurs the distinction between what is legally binding and what is not and thereby erodes international law as a whole – 'gliding bindness' as it has been called. (Mörth, 2005).

Soft law does not require the rigid definition, protracted procedures and parliamentary scrutiny of hard legislation. On the one hand avoiding these is alleged to better fit with a more societal and deliberative democracy than that offered by the model we tend to know, which is representative and majority based. There is an undoubted search for means of empowering citizens. In the United Kingdom a debate is beginning to get underway about a 'big society' with decentralisation and localism to the fore in which citizens come together spontaneously to provide services.

These concepts, however, risk running into difficulty because of their very lack of definition and clarity. They are unlikely to be robust enough to sit easily alongside machineries of central and local government which are structured constitutionally and are based upon legislation produced by an executive and financed through Parliament. A moment's thought shows that if public money is required to facilitate 'big society' systems then control will follow the cash – first control by the executive and ultimately control by Parliament. Otherwise established constitutions and developed democracy would count for nothing and taxpayers would be unable to maintain the use of their money and seek redress against abuse. It is everyone's guess how and whether spontaneous local groups using public funds can sit comfortably alongside traditional means of ensuring proper use of public money.

For empowerment techniques to work, and this is an important lesson from Sutherland, the

techniques of empowerment, like referenda for example, must be constitutionally established. The rules need to be clear and settled if they are to be credible. The rules of empowerment need to be hard rather than soft.

Ulrika Mörth put it very well.

“Democracy requires a clear division of authority, transparency, accountability and public debate. One problem with accommodating soft law to liberal democracy, therefore, is that the essential participants in policy formulation, based on soft law or measures that will result in soft law, are officials and other experts and not elected politicians. Inherent in soft law, furthermore, is a vagueness both in form (who is accountable) and in substance (the political commitments) that could impair accountability, transparency and public debate”. (Morth 2005).

The two systems may not be completely incompatible but delegation of power requires good definition, something at which soft law is poor. In our increasingly litigious societies and under the European Convention of Human Rights the right to judicial review of actions affecting citizens, and to appeal against provisions affecting them, are more and more prominent in all legal systems. Soft law techniques tend to sit very uncomfortably alongside appeal and judicial review because of their lack of rules. When powers are not properly defined it is difficult to see whether they have been exceeded.

Similar concerns to preserve constitutional accountability are currently visible in the United States. “One can have a government that functions without being ruled by functionaries, and a government that benefits from expertise without being ruled by experts” said Chief Justice Roberts this year *(Free Enterprise Fund V Public Company Accountability Oversight Board,* 56 US 2010). “Our constitution was adopted to enable the people to govern themselves, through their elected leaders. The growth of the Executive Branch, which now wields vast power and touches almost every aspect of daily life, heightens the concern that it may slip from the Executive’s control and thus from that of the people”, the xxx justice warned.

Soft law may also have slipped from control of the people. It has certainly escaped the modernisation of lawmaking and regulation in the better regulation processes. Hard law is now constrained by heavy requirements of consultation, impact assessment, judicial challenge as well as the rigours of the democratic law making process. Increasingly, as the European Commission noted recently, it is also subject to post-legislative review:

“All major existing policy instruments, whether expenditure programmes or regulatory measures, should be evaluated on a regular basis... to assess whether existing policies are

producing their intended results and - if not - propose the necessary, evidence-informed adaptations.... The Commission intends to launch pilot evaluations that would look at an entire policy sector to identify overlaps, gaps, inconsistencies, obsolete measures, excessive administrative burdens etc." (European Commission, 2010).

Although soft law is less likely to become encrusted with barnacles than hard law, is it not time that a similar overarching look reviewed key issues for soft law: where it is working and where not, where it should become proper law, where it lacks transparency or has been captured by officials or NGOs or lobbyists? Where it favours big powerful countries against smaller states?

Soft law is better seen as a transitional technique. It is a secondary concept. It can help test out policies in an evermore complex world, it can speed up decisions. It can facilitate experimentation, co-operation and flexibility. Yet it can never ultimately provide a stable basis for civil society. Soft law is at odds with the rule of law. Soft law is not a foundation of a constitutional order.

Soft law can conceal important and fundamental disagreements. It can conceal incompatibilities as in the case of a non-optimal currency area. Attempts as in the Stability and Growth Pact to create a hybrid of hard and soft law cause confusion leaving important groups dissatisfied. One finds the machinery toothless; the other unconstitutional. Neither are happy with the outcome.

The conclusion of this analysis is therefore that we should re-examine the way in which we make soft law. Should we live with hybridity? Should we attempt to formalise safeguards against the adverse consequences of non-traditional law making? An important starting point would be to review the spread of soft law in society, to map it and to attempt an estimation of its effectiveness. In my view we should impose a sunset clause on soft law. We should subject it to regular reviews against pre-established criteria.

Thereafter, in my submission, we should regard it as transitional. We should either legalise or drop. There is no satisfactory half way house by which effective safeguards could be applied to soft law systems. The purpose of soft law is often to bypass these very safeguards. Where we have guidelines, if they are satisfactory they should be turned in to laws. Where we have memoranda of understanding, protocols, codes of conduct we should turn them in due time into legal instruments or treaties.

The arguments that soft law techniques allow innovation and a faster pace of change may

be correct. But that does not mean that after three or five years these tools should not be revisited and, as I suggest, either legalised or dropped.

The case for entrenching soft law techniques as a permanent part of national or international law has not been made. It probably cannot be made in a manner compatible with legislative and treaty making processes on the one hand, and the enforcement, scrutiny and review elements of an effective constitution on the other.

Instead of allowing existing soft law to drift along and our societies to drift in to more soft law we should establish some boundaries. To borrow from the Code of Conduct on Business Taxation we should standstill, rollback or legalise.

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