

## **How To Produce Legitimate Global Norms In Commercial Law: The Case Of UNCITRAL's Legislative Guide On Insolvency Law.**

Terence C. Halliday  
American Bar Foundation

US scholars have appraised international private lawmaking institutions in terms of the efficiency of their product, their accountability and transparency, and how they have achieved success in unlikely circumstances. This presentation appraises them by another criterion – their legitimacy. I ask: what makes global making of commercial law legitimate? Why this question? Because, arguably, legitimacy or its absence affects the behavior of nation-states, it affects their orientations towards new global norms, and it affects the probability of adoption and compliance.

The paper is based on an empirical analysis of the production of the Legislative Guide on Corporate Insolvency Law that was approved by the United Commission on International Trade Law (UNCITRAL) in June 2004. The rapid passage of this Guide, in an area of commercial law thought to among the most resistant to global convergence, suggests that the scope of commercial lawmaking by international organizations may be greater than is often perceived and indicates several conditions under which global lawmaking is more likely to influence domestic lawmaking.

### **Background:**

The field of corporate insolvency law provides an excellent empirical site in which to examine the question of lawmaking legitimacy. It has been exceptionally difficult to design an acceptable framework for cross-border insolvency or to forge global consensus over universal norms for domestic insolvency law. Insolvency law has often been thought to be more deeply embedded in local cultural and policy preferences than other areas of commercial law. Moreover, there are enormous differences in the power and interests of global and national actors who might participate in the formulation of global norms and thus bedevil any prospect of a legitimate consensus. Yet, in relatively quick succession, the UN Commission on International Trade Law (UNCITRAL) has concluded a Model Law on Cross-Border Insolvency (1999) and a Legislative Guide on Corporate Insolvency (2004).

Both the Model Law and Legislative Guide were embroiled in politics of legitimacy. Over the past twenty-five years, repeated efforts have been made by private organizations (e.g., International Bar Association), international financial institutions (e.g., IMF, World Bank, Asian Development Bank), and international governance organizations (e.g., OECD) to develop protocols, principles, standards, and model laws. All foundered in part because of their legitimation deficits. They were perceived variously to be self-interested, to have expert but not representative warrants of authority (or vice versa), to be tainted by proximity to financial hegemony, such as the U.S., or by their coercive exercise of power, such as the IMF. The search for a solution became a quest for a legitimate forum and process. It is no accident that this quest ended with UNCITRAL.

This paper presents fragments of an empirical study of UNCITRAL's Working Group on Insolvency Law which labored from 1999 to 2004 to produce its Legislative

Guide on Corporate Insolvency.<sup>1</sup> I embed these fragments in a renewed scholarship on the legitimacy of international organizations and law-making institutions in political science and sociology. But I argue that legitimacy remains a key to the articulation of the global and local in the field of law-making. No matter how plausible, how technically sophisticated, how juridically sound, if norms are not considered legitimate they risk being ignored or repudiated.

### **On Legitimacy**

Legitimacy may be defined as “the normative belief by an actor that a rule or institution ought to be obeyed.”<sup>2</sup> When vested in a rule, legitimacy takes the shape of the belief by an actor that the rule ought to be obeyed. When vested in an institution, it manifests itself as the belief that the institution has the right to issue commands in its sphere of competence. Legitimacy is a *subjective* state, that is, it relies on a perception by an actor or audience that an institution or process should be obeyed.

But it should also be clear that legitimacy constitutes an alternative mode of social control and basis for action distinct from justice, or self interest, or favorable outcomes.

Hurd argues that three factors explain legitimacy of an international organization (IO).

1. Deliberation: actors have the opportunity to participate. This better distributes information; it alters perceptions of actor interests and may lead to shared understandings.
2. Procedural correctness: rules must be applied fairly and consistently to all participants, even if the rules themselves are not fair or just in themselves.
3. Effectiveness: an IO that is seen as successful in meeting its own goals will be seen as more legitimate. i.e., it gets things done, it must be taken seriously in its particular field. Together these add up to a sense of “rightness” about the power of an IO.

### **UNCITRAL’s Legitimation Strategies**

#### 1. Deliberation

UNCITRAL ensured its representative authority by inviting all UN member states to participate either as (a) regular delegates (initially thirty-six and later sixty member of the Commission), and (b) as observer delegates, although in practice no distinction was made between them in debate or decision-making. It also sought representation from IOs of interests salient to bankruptcy. UNCITRAL ensured its expert authority by integrating an array of international expert organizations, including professional associations, international financial institutions, private lawmaking bodies, and the like.

Paradoxically, by establishing the warrants of representative and expert authority, these intensified potential deliberation problems because they multiplied diversity among

---

<sup>1</sup> This paper draws on collaborative research undertaken with Bruce Carruthers (Northwestern University) on the globalization of corporate insolvency regimes and Susan Block-Lieb (Fordham University) on rule-making in the Working Group on Insolvency. Using the classic social science methodology of participant observation, I attended all but one of the formal meetings of the Working Group as a neutral observer, I repeatedly interviewed delegates and officials, and I tracked all speech turns by delegates in formal sessions. Whenever possible, I also kept abreast of informal and expert meetings outside the proceedings.

<sup>2</sup> The theoretical analysis of legitimacy benefits significantly from Ian Hurd (1999; forthcoming).

legal systems, widened asymmetries of power among nation-states, and heightened the prospect of clashes between competing forms of authority.

To solve these problems, UNCITRAL adopted mitigating deliberation techniques. For instance, the Working Group: (1) made enactability the touchstone of success, thus forsaking the optimal for the possible; (2) externalized some of the most public policy divisive issues that divide nations, such as priorities for the dispersion of assets in liquidations, most notably in the treatment of workers; (3) acted neutrally towards all legal traditions by not ostensibly privileging the concepts or practices or any; and (4) circulated drafting sections widely by internet, effectively opening them to all interested parties inside and outside the Working Group.

## 2. Procedure:

The UNCITRAL Working Group faced a problem even more acute than that in most national legislatures—the imbalance of power among nation-states far exceeds that among representatives in domestic politics. Domination by powerful states or interest groups—or capture—is ever possible. Yet capture directly subverts legitimacy, the very reason that the IMF and other IOs preferred to proceed through UNCITRAL.

The Working Group sought to mitigate this prospect by at least three mechanisms.

(1) since agenda-setting is a prime site for the exercise of power, UNCITRAL had two meetings in 1999 and 2000 to which all prior IOs with normmaking efforts in insolvency were invited together with some 150 participants from forty countries. These meetings set a global substantive course (the value of corporate reorganization), broad objectives, and both the substance (corporate insolvency) and form (legislative guide) of the law.

(2) since the Working Group incorporated almost all sides of the major fault-lines in insolvency law, it adopted participation protocols that included the appointment of officers (chairs, reporters) from smaller advanced or developing countries, a norm of participatory equality by any delegate (whether or not observers), and strict norms of speaking based on the temporal order in which delegations raised their “flags.”

(3) decision-making was by general consensus without a formal vote.

Analysis of speech turns shows generally that: (a) a wide range of delegates participated; (2) delegates participated disproportionately from certain countries (France, U.S.), from professional associations (e.g., IBA, INSOL, ABA, III), and from advanced countries.

## 3. Effectiveness:

A legitimate institution must show it can succeed. UNCITRAL has a long track record of successful products, not least the Model Law of Cross-Border Insolvency that had been produced by this Working Group. A national corporate bankruptcy law presented its most formidable challenge. It responded by employing a set of formal strategies to conclude successfully production of its Legislative Guide.

I will discuss two main formal strategies, both of which turn on repertoires of outputs.

(1) UNCITRAL has developed a *repertoire of technologies*. That is, it can ratchet up or down the rigors of formulation or implementation of norms in response to the exigencies of topic, time constraints, and global diversity. While UNCITRAL is best known for its *conventions*, where countries must negotiate a multilateral treaty that is binding on

nation-states and brooks no deviation, and *model laws*, which offer a global standard that nation-states are encouraged to observe but are not bound to do so, the WG on Insolvency for the first time produced a free-standing (i.e., not connected to a Model Law) *legislative guide*, which was intended to “set out a number of issues often addressed in national laws and regulations”, discuss the merits of proceeding in one or another direction, and “provide a set of possible legislative solutions.” In short, by relaxing the formal demands of the legal technology, UNCITRAL could reach consensus on global norms that would have been impossible with a model law or convention.

(2) UNCITRAL has developed a *repertoire of norms*. Within the Legislative Guide on Insolvency, the WG generated a differentiated repertoire of norms that varied on two dimensions.

First, Susan Block-Lieb has identified four clusters of recommendations or “rules.” (1) *Policy recommendations* identify and affirm substantive commercial norms. (2) *Imperative recommendations* propose that national legislatures take specific types of action whose content is given. These include *substantive recommendations* (there should be a rule [about the substantive entitlements of participants in an insolvency proceeding] that says [X]); *procedural recommendations* (there should be a rule [about how an insolvency proceeding should be conducted] that says [X]); and *conditional recommendations* (if you have a rule [which is not mandatory] it should have [X] form). (3) *Constraining recommendations* are not explicitly directive as to particular courses of action but they are conducive to convergence, often by pointing in a direction and then giving choices. These include *baseline recommendations* (there should be a rule on [Y], and its minimal substance should include [R,S,T]; ); *norms of minimalism* (if there is to be a rule on [X], or an exception to the rule on [X], it should be kept to a minimum); *permissive recommendations* (a country may adopt a rule that includes [X], [Y] and [Z] and some options will be given as to which might be appropriate). Supporting these are footnoted materials and commentary with no correlative recommendation. (4) *Specifying recommendations* sharpen the focus on any law that happens to be on books. These include *architectural recommendations* (there should be rule on these topics, but it does not specify what the rule should be); and *norms of disclosure* (a specific rule on [Y] should have the formal properties of [X]).

Second, there are variable levels of specificity and generality within most types of recommendations. Or, reduced to the dichotomy found in scholarship on private lawmaking, each of these three types of recommendations might result in a national legislature adopting a bright-line rule, should it be appropriate to the circumstance, or a principle.

Through the flexibility obtained by these two dimensions of norms, UNCITRAL concomitantly can facilitate convergence or predictability, solve its own legitimation problems of inclusiveness and expertise, and avoid either extreme of enunciating norms that are effectively meaningless or are so precise as to engender a backlash through encroachment on sovereignty. In other words, adaptation to the sensitivities of sovereignty offers another basis of global legitimation.

By choosing a technology (i.e., a legislative guide) that permits a great deal of cross-national variation, and by creating the flexibility of recommendation-types by levels of abstraction, the combination of the two has given UNCITRAL great flexibility in dealing with any issue, no matter how divisive. The recommendation type or level of

specificity is varied depending both on the difficulty of obtaining consensus in normmaking and in the degrees of freedom thought desirable for national legislatures. The result is a successful Legislative Guide in an area of commercial law thought to be not susceptible to global convergence.

**Conclusion:**

What makes commercial lawmaking legitimate in global forums? UNCITRAL's Working Group on Insolvency employed three sets of strategies which are consistent with current theory of legitimacy in IOs: strategies of deliberation, procedure, and effectiveness.

By generating a legitimate product UNCITRAL accomplishes several things. First, it offers a more sophisticated repertoire of normmaking than a simple notion of precise versus vague rules. Second, it increases the probability that global norms will be institutionalized by domestic legislatures. Third, it treads lightly on national sovereignty for it enables domestic legislatures ample room for maneuver within the spirit of the guide such that they can decide on levels of rule-specificity best adapted to local situations. Fourth, it presses global commercial practice around bankruptcy towards convergence without harmonization. Fifth, it weds global lawmaking to domestic implementation through partnerships with the IOs it coopted in the process (cooptation might be thought to be reciprocal here). And, finally, it sets in train an iterative process of normmaking or recursivity between global normmaking institutions and national legislatures.

By adopting a sliding scale of specificity or abstractness of recommendations, UNCITRAL breaks out of the conceptual straitjacket that posits an either/or of principles versus rules, where principles are held to be less desirable for commercial regulation. Effectively, UNCITRAL follows in practice the powerful critique of the assumptions about principles and rules made by Braithwaite and Drahos (2000) on the basis of the arguably the most extensive empirical research undertaken on global business regulation. Braithwaite (2001) concludes that in market circumstances where change is rapid, economic stakes are high, and situations are complex, principles deliver more consistency than rules.

Close empirical observation and analysis of the UNCITRAL Working Group further suggests that it is not susceptible to some of the critiques offered by international private lawmaking scholars. To style UNCITRAL's Working Groups as "private" legislatures seems doubtful. This Working Group was not dominated by academics or technocrats, nor was it captured by dominant actors (e.g., IFIs, US); it did not produce take-it or leave-it models that inhibit full debate in normal domestic lawmaking; and it certainly did not reinforce the status quo.

As a result of its adroit combination of legitimation strategies, UNCITRAL and organizations like it can "reach" areas of commercial law previously thought to be outside their capabilities and beyond their scope. This suggests that global lawmaking is likely to expand inexorably in business regulation and that an increasing amount of US and international legal practice will take place in the shadow of this lawmaking.