Special Issue
Democracy and Financial Order—Legal Perspectives

The Limits of Law (and Democracy) in the Euro Crisis: An Approach from Systems Theory

By Lars Viellechner[*]

Abstract

The Article attempts to explore the fate of law and democracy in the euro crisis from the sociological perspective of systems theory. It consecutively ascertains the performance, the relevance, and the function of the law with regard to the current practice of restructuring sovereign debt in the euro area. While novel forms of regulation such as the European Stability Mechanism attest a remarkable assertiveness of the law, they cannot effectively command economic recovery and must cede to economic imperatives for their part. Under such circumstances, the law can no longer adequately fulfill its function to counterfactually secure normative expectations. Nevertheless, the regulatory experiments in the euro crisis may not be regarded as undemocratic. Rather, the heterarchical processes of mutual observation, recognition, and contestation among the various constituencies involved, including representatives of governments, institutions of the European Union, central banks, national parliaments and peoples via referenda, as well as European and national courts, provide some substitute for the lack of elections and parliamentary decision-making at the European level.

[*] Dr. iur. (Berlin), LL.M. (Yale), lic. dr. (Paris II). Associate Professor of Constitutional Law, Constitutional Theory, Legal Philosophy, and Transnational Law, University of Bremen. Email: lars.viellechner@uni-bremen.de.

https://doi.org/10.1017/S2071832200021441 Published online by Cambridge University Press

A. Introduction

The various supranational and international instruments that aim to ensure the stability of the euro and restructure the sovereign debt of some of the member states of the European Union (EU) in the face of the current financial crisis are not only highly complex in their construction and interaction so that even experts have difficulty in comprehending them.[1] Their legality is also much contested. Meanwhile, the Court of Justice of the European Union (CJEU)[2] and some national constitutional courts[3] have decided on the compatibility of some important rescue measures, notably the establishment of the European Stability Mechanism (ESM) and the Outright Monetary Transactions (OMT) program of the European Central Bank (ECB), with European and national constitutional law respectively, largely approving of them. Nonetheless, each subsequent step towards restructuring sovereign debt within the euro area raises new issues of legality. Thus, it was recently discussed if a debt "haircut" could be made part of additional financial assistance facilities to support Greece.[4] Apart from that, some legal scholars have tried to develop a set of abstract legal principles against which to measure the legitimacy of sovereign debt restructuring in the future.[5]

As a sociological approach, systems theory cannot contribute to the normative debate on the legality and legitimacy of financial market regulation in general and sovereign debt restructuring in particular. It cannot even engage in any kind of "rational reconstruction"[6]

---

[1] For an overview of the legal instruments, *see* Alberto de Gregorio Merino, *Legal Developments in the Economic and Monetary Union During the Debt Crisis: The Mechanisms of Financial Assistance*, 49 COMMON MKT. L. REV. 1613 (2012).

[2] *See* Case C-62/14, Gauweiler and Others v. Deutscher Bundestag, ECLI:EU:C:2015:400; Case C-370/12, Pringle v. Government of Ireland, ECLI:EU:C:2012:756.

[3] For the German perspective, *see* Bundesverfassungsgericht [BVerfG] [Federal Constitutional Court], June 21, 2016, Case No. 2 BvR 2728/13 et al., http://www.bverfg.de/e/rs20160621_2bvr272813.html; March 18, 2014, 135 ENTSCHEIDUNGEN DES BUNDESVERFASSUNGSGERICHTS [BVERFGE] 317; Jan. 14, 2014, 134 ENTSCHEIDUNGEN DES BUNDESVERFASSUNGSGERICHTS [BVERFGE] 366; Sept. 12, 2012, 132 ENTSCHEIDUNGEN DES BUNDESVERFASSUNGSGERICHTS [BVERFGE] 195; June 19, 2012, 131 ENTSCHEIDUNGEN DES BUNDESVERFASSUNGSGERICHTS [BVERFGE] 152; Feb. 28, 2012, 130 ENTSCHEIDUNGEN DES BUNDESVERFASSUNGSGERICHTS [BVERFGE] 318; Sept. 7, 2011, 129 ENTSCHEIDUNGEN DES BUNDESVERFASSUNGSGERICHTS [BVERFGE] 124.

[4] *See* Armin von Bogdandy et al., *Verlustrisiko: Griechenlands Schuldenlast kann und muss im Euroraum erleichtert werden*, FRANKFURTER ALLGEMEINE ZEITUNG (July 23, 2015), http://www.faz.net/aktuell/politik/staat-und-recht/griechenland-krise-schuldenschnitt-auch-ohne-grexit-moeglich-13715803.html; Armin Steinbach, *The "Haircut" of Public Creditors Under EU Law*, 12 EUR. CONST. L. REV. 223.

[5] *See* Armin von Bogdandy & Matthias Goldmann, *Sovereign Debt Restructurings as Exercises of International Public Authority: Towards a Decentralized Sovereign Insolvency Law*, *in* SOVEREIGN FINANCING AND INTERNATIONAL LAW: THE UNCTAD PRINCIPLES ON RESPONSIBLE SOVEREIGN LENDING AND BORROWING 39 (Carlos Espósito et al. eds., 2013).

[6] Matthias Goldmann & Silvia Steininger, *A Discourse Theoretical Approach to Sovereign Debt Restructuring: Towards a Democratic Financial Order*, in this issue.

https://doi.org/10.1017/S2071832200021441 Published online by Cambridge University Press

that would carve out the normative presuppositions underlying the contemporary practice of financial regulation and, hence, oscillate between the empirical and the normative. It can only describe and analyze the role that the law—and democratic political lawmaking—might assume in view of financial crisis. Such an endeavor is not futile. It may reveal systemic deficiencies in the current practice of financial regulation and thus help policy-makers and lawyers acknowledge which avenues to follow in order to reach their aims.

Nevertheless, the analysis remains difficult because the version of systems theory submitted by Niklas Luhmann,[7] which serves as a tool of analysis here, has never expressly dealt with financial crisis. Neither has Luhmann comprehensively explored international or European law, although he left some short, yet clear-sighted presumptions on the fate of law in the further evolution of world society, which he had already started formulating at the beginning of the 1970s.[8] Only recently have some of Luhmann's followers started to discuss the role of law in the current financial crisis, but their studies focus on the possibilities of political-legal intervention on the private side of financial markets while altogether ignoring the topic of sovereign debt restructuring, which supposedly requires a different assessment.[9]

Hence, the present attempt at analyzing the role of law—and democratic political lawmaking—in coping with the euro crisis from the perspective of systems theory may only draw on some of Luhmann's more general insights concerning the relationship of law, politics, and the economy. In so doing, it cannot claim to deliver an authoritative interpretation of Luhmann's work. It can only offer what appears to be a plausible reading of this version of systems theory.

The survey will consecutively ascertain the performance (B.), the relevance (C.), and the function of the law (D.) with regard to the current practice of restructuring sovereign debt in the euro area. All three terms are employed in everyday language, but they have specific meanings in systems theory. The sociological analysis will also yield some observations on the legitimacy of the regulatory practice in the euro crisis, even though it does not allow for a normative appraisal (E.).

---

[7] *See generally* NIKLAS LUHMANN, SOCIAL SYSTEMS (John Bednarz trans., Stanford University Press 1995) (1984).

[8] *See* Niklas Luhmann, *Die Weltgesellschaft*, 57 ARCHIV FÜR RECHTS- UND SOZIALPHILOSOPHIE 1 (1971); NIKLAS LUHMANN, A SOCIOLOGICAL THEORY OF LAW 255–64 (Elizabeth King & Martin Albrow trans., Routledge & Kegan Paul 1985) (1972); NIKLAS LUHMANN, LAW AS A SOCIAL SYSTEM 479–90 (Klaus A. Ziegert trans., Oxford University Press 2004) (1993).

[9] *See* the contributions in THE FINANCIAL CRISIS IN CONSTITUTIONAL PERSPECTIVE: THE DARK SIDE OF FUNCTIONAL DIFFERENTIATION (Poul F. Kjaer et al. eds., 2011).

https://doi.org/10.1017/S2071832200021441 Published online by Cambridge University Press

B. Performance

The first observation relates to the performance that the law may achieve with regard to shaping the financial market in general and restructuring sovereign debt in particular. Such a capacity for achievement crucially depends on the relationship between the various social systems, especially politics, law, and the economy. In this respect, it is necessary to explain some of the basic assumptions of systems theory as a social theory. According to Luhmann's most fundamental claim, modern society consists of various social systems, such as religion, politics, law, the economy, the sciences, and the arts that operate self-referentially according to their own rationality. While each system fulfills a function that is indispensable to society as a whole, it cannot directly influence, but only irritate the others. Consequently, external information or stimulation may only be processed according to the inner logic of each system.[10] For Luhmann, therefore, any attempt at social steering by means of politics and law was doomed to fail. In particular, he regarded the "welfare state,"[11] which tried to assume a universal responsibility for prosperity in all spheres of social life, as a useless "effort to inflate the cows in order to get more milk."[12]

Still, Luhmann conceded that social systems might presuppose certain features of their environments and rely on them structurally. For example, he assumed that the political and legal systems were linked through a "structural coupling"[13] in the form of the constitution, which allows for them to have a certain impact on each other.[14] He also admitted that politics and law, in their peculiar conjunction through the constitution, "imply the action capacity of the system more than any other structures" and therefore serve as "the primary developmental factor or risk carrier of societal development."[15] In this regard, he came close to Jürgen Habermas, who, when further elaborating on his discourse theory of law and democracy "connect[ed] with an objectifying sociological approach that regards the political system neither as the peak nor the center, nor even as the structuring model of society, but as just one action system among others." Thus, he

[10] *See* LUHMANN, SOCIAL SYSTEMS, *supra* note 7, at 12–58.

[11] Asa Briggs, *The Welfare State in Historical Perspective*, 2 EUR. J. SOC. 221 (1961); NIKLAS LUHMANN, POLITICAL THEORY IN THE WELFARE STATE (John Bednarz trans., De Gruyter) (1981).

[12] Niklas Luhmann, *Der Staat des politischen Systems: Geschichte und Stellung in der Weltgesellschaft*, *in* PERSPEKTIVEN DER WELTGESELLSCHAFT 345, 369 (Ulrich Beck ed., 1998) (my translation).

[13] Niklas Luhmann, *Operational Closure and Structural Coupling: The Differentiation of the Legal System*, 13 CARDOZO L. REV. 1419 (1992).

[14] *See* Niklas Luhmann, *Verfassung als evolutionäre Errungenschaft*, 9 RECHTSHISTORISCHES J.176 (1990).

[15] LUHMANN, A SOCIOLOGICAL THEORY OF LAW, *supra* note 8, at 259–60.

https://doi.org/10.1017/S2071832200021441 Published online by Cambridge University Press

admitted that politics may, through the medium of law, only provide "a kind of surety" for solving problems of society as a whole.[16]

Gunther Teubner and Helmut Willke took a similar diagnosis as a point of departure for imagining a "reflexive law"[17] that, albeit unable to govern other social systems, may at least stimulate processes of self-reflection within them in order to allow for their mutual consideration and hence social integration in the absence of a central steering agency. Yet, Luhmann was not convinced. For the orthodox strand of systems theory, it is "inconceivable that law could control and regulate the autopoiesis of all social systems,"[18] even in the extenuated sense of a regulation of self-regulation. In this view, none of the social systems may assume a superordinate position, not even as a catalyst or moderator to facilitate coordination among them. It is therefore impossible that political-legal intervention could in any way channel the economic system and effectively cure the deficiencies of a failing financial market.

There may only be hope for a successful "self-constitutionalization"[19] of the economic system. As Teubner has recently demonstrated with regard to the example of plain money reform in the current financial crisis, such a transformation could not only be induced by external pressure, but also by the near-death experience of "hitting the bottom."[20] Supposedly, the relevant parts of society, in this case the financial market, will be able to develop an extraordinary strength that allows them to pull themselves out of the swamp by their own bootstraps when facing an imminent existential threat. A self-regulation of this kind, however, is highly demanding and extremely fragile. It requires the economic system to develop a capacity for self-reflection ultimately provoking a willingness to engage in self-restraint, which can neither be induced nor ensured from outside.

The situation appears to be different when it comes to restructuring the sovereign debt of nation-states through supranational and international law, as currently practiced in the EU.

---

[16] JÜRGEN HABERMAS, *Three Normative Models of Democracy*, *in* THE INCLUSION OF THE OTHER: STUDIES IN POLITICAL THEORY 239, 251 (Ciaran Cronin trans., Massachusetts Institute of Technology Press 1998) (1996).

[17] Gunther Teubner, *Substantive and Reflexive Elements in Modern Law*, 17 LAW & SOC'Y REV. 239, 266 (1983); Helmut Willke, *Societal Guidance Through Law?*, *in* STATE, LAW, AND ECONOMY AS AUTOPOIETIC SYSTEMS: REGULATION AND AUTONOMY IN A NEW PERSPECTIVE 353, 366 (Gunther Teubner& Alberto Febbrajo eds., 1992).

[18] Niklas Luhmann, *Some Problems with "Reflexive Law," in* STATE, LAW, AND ECONOMY AS AUTOPOIETIC SYSTEMS: REGULATION AND AUTONOMY IN A NEW PERSPECTIVE 389, 397 (Gunther Teubner & Alberto Febbrajo eds., 1992).

[19] Gunther Teubner, *Societal Constitutionalism: Alternatives to State-Centered Constitutional Theory?*, *in* TRANSNATIONAL GOVERNANCE AND CONSTITUTIONALISM 3, 15 (Christian Joerges et al. eds., 2004). For more detail, *see* GUNTHER TEUBNER, CONSTITUTIONAL FRAGMENTS: SOCIETAL CONSTITUTIONALISM AND GLOBALIZATION (Gareth Norbury trans., Oxford University Press) (2012).

[20] Gunther Teubner, *A Constitutional Moment? The Logics of "Hitting the Bottom," in* THE FINANCIAL CRISIS IN CONSTITUTIONAL PERSPECTIVE: THE DARK SIDE OF FUNCTIONAL DIFFERENTIATION 3 (Poul F. Kjaer et al. eds., 2011).

https://doi.org/10.1017/S2071832200021441 Published online by Cambridge University Press

In this case, regulation does not encounter insurmountable systemic boundaries because both regulatory means and targets lie within the reach of the political and legal systems. Nation-states as political entities may readily engage with other nation-states by employing the political-legal instruments of international treaties. They may also be able and willing to comply with the secondary legislation of the supranational organizations to which they are members. At the same time, they have the means of administrative law at their disposal to implement the political reforms of public spending that supranational and international law might call for. Indeed, the member states of the EU whose currency is the euro have proved a remarkable capacity and willingness to solve problems by establishing, and complying with, the law of newly erected international financial institutions such as the ESM.[21]

Nonetheless, the effectiveness of political-legal attempts at restructuring sovereign debt may be impaired by two factors. First, whether the reforms of public spending that are politically agreed upon and legally implemented will eventually succeed depends on a favorable development of the economy at large. Politics and law, however, cannot command economic recovery. At this point, the systemic boundaries reoccur. If at all, the legal restructuring of sovereign debt may take the form of what is called "purposive programs," as opposed to "conditional programs."[22] While conditional programs clearly define the conditions and effects of a certain rule, purposive programs solely name a distinctive goal to be reached in a particular case and some aspects to be considered in the process of decision-making, while the path to realizing the goal also hinges on various external circumstances. The conditionality attached to the financial assistance facilities according to Article 13(3) of the ESM Treaty provides an illustrative example of such purposive programs—the term "conditionality" should not cause confusion here.[23] For example, the memorandum of understanding that implements the third assistance program to support Greece under the ESM builds on four abstract goals: (1) restoring fiscal sustainability; (2) safeguarding financial stability; (3) growth, competitiveness, and investment; and (4) a modern state and public administration. It also enlists certain sectors of reform and some specific measures to be adopted by the Greek government in this respect, including reorganization in the areas of taxation, pensions, health care, and justice, among others.[24] Nevertheless, there is no guarantee that the political goals

[21] *See* Paul Craig, *Economic Governance and the Euro Crisis: Constitutional Architecture and Constitutional Implications*, *in* THE CONSTITUTIONALIZATION OF EUROPEAN BUDGETARY CONSTRAINTS 19 (Maurice Adams et al. eds., 2014); FEDERICO FABBRINI, ECONOMIC GOVERNANCE IN EUROPE: COMPARATIVE PARADOXES, CONSTITUTIONAL CHALLENGES (2016).

[22] NIKLAS LUHMANN, RECHT UND AUTOMATION IN DER ÖFFENTLICHEN VERWALTUNG: EINE VERWALTUNGSWISSENSCHAFTLICHE UNTERSUCHUNG 36 (1966).

[23] *See* Treaty Establishing the European Stability Mechanism, Feb. 2, 2012, art. 13(3), http://www.esm.europa.eu/about/legal-documents/ESM%20Treaty.htm [hereinafter ESM].

https://doi.org/10.1017/S2071832200021441 Published online by Cambridge University Press

stipulated in the program will in fact be reached. Even if faithfully realized, the political reforms may have adverse effects on the economic system, while changing economic or other social circumstances may thwart their realization in the first place. Moreover, as purposive programs grant a generous amount of leeway in their application, judicial control is hampered so that the law loses much of its force.

Second, it is possible that the parties to an international treaty that restructures sovereign debt will not keep their promises. As a matter of fact, international law has long suffered from a lack of authority because the nation-states are simultaneously its authors and addressees. Many commentators have even denied its legal character on these grounds.[25] To be sure, it is nowadays well established that "almost all nations observe almost all principles of international law and almost all of their obligations almost all of the time."[26] Under conditions of economic hardship, however, the debtor states may have no alternative but to disregard their legal obligations. Thus, several member states of the EU have exceeded the deficit thresholds of the Stability and Growth Pact (SGP) in the past.[27]

Apart from that, some observers recognize a significant difference in compliance with the law between member states of the EU from the north and from the south.[28] It is not clear whether this allegation can stand up to objections but, if it is accepted, such divergence can be explained by persisting differences in legal cultures and mentalities that even systems theory acknowledges. Although Luhmann generally assumed a differentiation of social systems on a global scale, he admitted that the political and legal systems of world society are still characterized by a "segmental, secondary differentiation"[29] into nation-states, which entails that, regarding the law, "enormous differences in the different regions of the globe cannot be overlooked."[30] Consequently, as neither upswings in the economy nor changes in mentality may be imposed by command and control, there

[24] *See* Memorandum of Understanding Between the European Commission Acting on Behalf of the European Stability Mechanism and the Hellenic Republic and the Bank of Greece, EUR. COMM'N (Aug. 19, 2015), http://ec.europa.eu/economy_finance/assistance_eu_ms/greek_loan_facility/pdf/01_mou_20150811_en.pdf.

[25] *See, e.g.*, JOHN AUSTIN, THE PROVINCE OF JURISPRUDENCE DETERMINED 208 (1832). For an overview of the various approaches, *see* GUSTAV ADOLF WALZ, WESEN DES VÖLKERRECHTS UND KRITIK DER VÖLKERRECHTSLEUGNER (1930).

[26] LOUIS HENKIN, HOW NATIONS BEHAVE: LAW AND FOREIGN POLICY 47 (2d ed. 1979).

[27] *See* Overview of Ongoing and Closed Excessive Deficit Procedures, EUR. COMM'N (Sept. 23, 2016), http://ec.europa.eu/economy_finance/economic_governance/sgp/corrective_arm/index_en.htm.

[28] *See* Karl-Heinz Ladeur, *Diesseits der Rechtsgemeinschaft: Die "instituierende Gewalt" der sozialen Regeln und die Grenzen der europäischen Integration*, *in* EUROPA: KRISE, UMBRUCH UND NEUE ORDNUNG 139, 148–51 (Stefan Kadelbach & Klaus Günther eds., 2014).

[29] LUHMANN, LAW AS A SOCIAL SYSTEM, *supra* note 8, at 487.

[30] *Id.* at 481. For an illustration regarding the case of Brazil, *see* MARCELO NEVES, VERFASSUNG UND POSITIVITÄT DES RECHTS IN DER PERIPHEREN MODERNE: EINE THEORETISCHE BETRACHTUNG UND EINE INTERPRETATION DES FALLS BRASILIEN (1992).

remains serious doubt as to whether the political-legal attempts at restructuring sovereign debt in the euro area will eventually succeed.

C. Relevance

The second observation concerns the relevance that law may retain in facing the euro crisis. Exposing the argument requires clarifying the basic function of law with regard to society, that is, the question of which problem of society is solved by the differentiation of a specialized legal system. According to Luhmann, each social system only fulfills one particular function for which there is no equivalent, whereas a social system may render various performances with regard to society for which other social systems may well offer alternatives.[31] For example, dispute resolution is only a performance, not a function, of the legal system because arbitrators and mediators may also provide it instead of courts. In this understanding, the one and only function of the law is the counterfactual "stabilization of normative expectations."[32] While normative expectations are upheld even if someone acts against them, cognitive expectations are adapted to reality in cases of disappointment. The latter are hence characterized by a preparedness to learn.[33]

Against this background, Luhmann suspected that social structures marked by a cognitive style of orientation would gradually supersede those showing a normative orientation in the evolution of world society.[34] As he explained, there has long been a preference for normative mechanisms of orientation because of their stabilizing function. For this reason, he claimed, such social systems as religion, politics, and law had assumed a predominant role in the past. By contrast, Luhmann found that those social systems that open up and support worldwide social relations, such as the economy, science, and technology, clearly show a cognitive style of orientation. A "shift of evolutionary primacy from normative to

[31] *See* LUHMANN, LAW AS A SOCIAL SYSTEM, *supra* note 8, at 142–72.

[32] *Id.* at 148.

[33] *See* LUHMANN, A SOCIOLOGICAL THEORY OF LAW, *supra* note 8, at 31–40. For an obnoxious example of the distinction between normative and cognitive expectations, *see id.* at 33:

> Suppose, for example, one is waiting for a new secretary. This situation contains both cognitive and normative components of expectation. To be sure, the fact that she could be young, pretty and blonde may be cognitively expected; but in these respects it is necessary to adapt to disappointments, i.e. not to insist on blonde hair, ask for it to be dyed, etc. However, it is normatively expected that she should achieve something.

[34] *See* Luhmann, *Weltgesellschaft*, *supra* note 8, at 10–17; LUHMANN, A SOCIOLOGICAL THEORY OF LAW, *supra* note 8, at 261–64.

https://doi.org/10.1017/S2071832200021441 Published online by Cambridge University Press

cognitive mechanisms"[35] of orientation therefore appeared obvious to him. He even insinuated

> that—in relation to further developmental possibilities—the provision of normative, political-legal mechanisms, which were passed down from high cultures, was a flawed specialisation of human development from which further evolution could not ensue; that we have, with them, established ourselves at a level of the system from which the evolution of social systems toward higher complexity cannot be continued.[36]

At first glance, however, the developments during the current euro crisis do not appear to attest to Luhmann's conjecture on the withering of law in the evolution of world society. At least with regard to European financial governance, a "de-juridification,"[37] or a move to "informal governance,"[38] is barely perceivable. Certainly, the attempts at ensuring the financial stability of the euro area have fundamentally altered the institutional and constitutional structure of the EU.[39] Not only have the European Council and the euro group become the center of political decision-making, while the latter is indeed an informal body whose meetings are highly nontransparent.[40] This "new intergovernmentalism"[41] has also created a new layer of international law that supplements EU law.[42] Most notably, an international treaty between the member states

[35] LUHMANN, A SOCIOLOGICAL THEORY OF LAW, *supra* note 8, at 262.

[36] *Id.* at 261.

[37] Christian Joerges, *Law and Politics in Europe's Crisis: On the History of the Impact of an Unfortunate Configuration*, 21 CONSTELLATIONS 249, 251 (2014).

[38] MAREIKE KLEINE, INFORMAL GOVERNANCE IN THE EUROPEAN UNION: HOW GOVERNMENTS MAKE INTERNATIONAL ORGANIZATIONS WORK (2013).

[39] *See* KAARLO TUORI & KLAUS TUORI, THE EUROZONE CRISIS: A CONSTITUTIONAL ANALYSIS (2014); ALICIA HINAREJOS, THE EURO AREA CRISIS IN CONSTITUTIONAL PERSPECTIVE (2015).

[40] *See* UWE PUETTER, THE EUROPEAN COUNCIL AND THE COUNCIL: NEW INTERGOVERNMENTALISM AND INSTITUTIONAL CHANGE (2014); UWE PUETTER, THE EUROGROUP: HOW A SECRETIVE CIRCLE OF FINANCE MINISTERS SHAPE EUROPEAN ECONOMIC GOVERNANCE (2006).

[41] Christopher J. Bickerton et al., *The New Intergovernmentalism: European Integration in the Post-Maastricht Era*, 53 J. COMMON MKT. STUD. 703 (2015); *see also* Sergio Fabbrini, *Intergovernmentalism and Its Limits: Assessing the European Union's Answer to the Euro Crisis*, 46 COMP. POL. STUD. 1003 (2013).

[42] *See* Angelos Dimopoulos, *The Use of International Law as a Tool for Enhancing Governance in the Eurozone and Its Impact on EU Constitutional Integrity*, *in* THE CONSTITUTIONALIZATION OF EUROPEAN BUDGETARY CONSTRAINTS 41

https://doi.org/10.1017/S2071832200021441 Published online by Cambridge University Press

of the EU whose currency is the euro established the ESM.[43] At the same time, some of the newly erected international institutions borrow certain organs of the EU in order to reach their aims, thereby generating a new kind of hybrid law that combines elements of both international and EU law.[44] In particular, the ESM assigns several tasks to the European Commission, the ECB, and the CJEU, in addition to providing for a close cooperation with the International Monetary Fund (IMF).[45] In this way, the respective institutions also attain a preponderant role in European financial governance.[46] Yet none of these transformations results in a decline of law. On the contrary, the recourse to the cumbersome legal constructions here described attests that the member states of the EU whose currency is the euro undertake all efforts to frame their attempt at ensuring the financial stability of the euro area in terms of law.

Even in the rare instances in which European financial governance, for lack of alternatives, resorts to instruments of soft law, a strong normativity prevails. For example, Article 13(3) of the ESM Treaty stipulates that memoranda of understanding shall detail the conditionality of the financial assistance facilities that are granted to ESM member states.[47] Although these agreements specify the general terms of the ESM Treaty on a particular occasion, they are not, in themselves, legally binding.[48] Nevertheless, they are perceived as strictly obligatory because the ESM may refuse to release subsequent payments in the case of non-compliance.

(Maurice Adams et al. eds., 2014); R. Alexander Lorz & Heiko Sauer, *Ersatzunionsrecht und Grundgesetz: Verfassungsrechtliche Zustimmungsgrundlagen für den Fiskalpakt, den ESM-Vertrag und die Änderung des AEUV*, 65 DIE ÖFFENTLICHE VERWALTUNG 573 (2012).

[43] *See* Treaty Establishing the European Stability Mechanism, Feb. 2, 2012, http://www.esm.europa.eu/about/legal-documents/ESM%20Treaty.htm [hereinafter ESM].

[44] *See* Steve Peers, *Towards a New Form of EU Law?: The Use of EU Institutions Outside the EU Legal Framework*, 9 EUR. CONST. L. REV. 37 (2013); Andreas Fischer-Lescano & Lukas Oberndorfer, *Fiskalvertrag und Unionsrecht: Unionsrechtliche Grenzen völkervertraglicher Fiskalregulierung und Organleihe*, 66 NEUE JURISTISCHE WOCHENSCHRIFT 9 (2013).

[45] *See* ESM arts. 13, 37–38.

[46] *See* Michael W. Bauer & Stefan Becker, *The Unexpected Winner of the Crisis: The European Commission's Strengthened Role in Economic Governance*, 36 J. EUR. INTEGRATION 213 (2014); Thomas Beukers, *The New ECB and Its Relationship with the Eurozone Member States: Between Central Bank Independence and Central Bank Intervention*, 50 COMMON MKT. L. REV. 1579 (2013).

[47] *See* ESM art. 13(3).

[48] *See* Michael Schwarz, *A Memorandum of Misunderstanding—The Doomed Road of the European Stability Mechanism and a Possible Way Out: Enhanced Cooperation*, 51 COMMON MKT. L. REV. 389 (2014); Maria Meng-Papantoni, *Legal Aspects of the Memoranda of Understanding in the Greek Debt Crisis*, 18 ZEITSCHRIFT FÜR EUROPARECHTLICHE STUDIEN 3 (2015).

https://doi.org/10.1017/S2071832200021441 Published online by Cambridge University Press

A pronounced reliance on the law also resurfaces with regard to judicial control of the euro crisis. Indeed, it appears that courts have never before been called upon as extensively to monitor and shape a financial crisis.[49] Plaintiffs have turned to any competent jurisdiction in any possible way. Not only have they challenged the public law framework of sovereign debt restructuring in the euro area before both European and national constitutional courts,[50] but they have also sued debtor states in civil proceedings.[51]

Nevertheless, the smashing force and sustained impact of the euro crisis demonstrate how far a globalized economy may gain predominance over all other social systems including the law. Although the economy does not supersede the law, legal regulation and control of the euro crisis become highly dependent on extra-legal knowledge. Certainly, the functioning of the explicit rules and principles of law has always built upon an underlying infrastructure of social norms and informal conventions that store the implicit knowledge and practical experience dispersed in society.[52] Moreover, the modern welfare state, which does not only limit itself to averting imminent dangers for its citizens but more expansively assumes the task of risk precaution,[53] has to increasingly rely on scientific findings and technical expertise when taking political decisions. Only in this way can it avoid measures that will miss their targets. It therefore has to cooperate with various non-state actors that gain privileged positions as they participate in the process of law formation.[54]

When it comes to regulating the financial market and restructuring sovereign debt, however, extra-legal knowledge almost entirely determines political decisions that result in legal norms. This development is unavoidable because the assessment and evaluation of what action should be taken in order to achieve financial stability crucially depends on both economic expertise and practical experience in the respective areas of reform. Consequently, Article 13(1) of the ESM Treaty assigns the tasks of assessing the existence

[49] *See* Samo Bardutzky & Elaine Fahey, *Who Got to Adjudicate the EU's Financial Crisis and Why? Judicial Review of the Legal Instruments of the Eurozone*, *in* THE CONSTITUTIONALIZATION OF EUROPEAN BUDGETARY CONSTRAINTS 341 (Maurice Adams et al. eds., 2014); Alicia Hinarejos, *The Role of Courts in the Wake of the Eurozone Crisis*, *in* BEYOND THE CRISIS: THE GOVERNANCE OF EUROPE'S ECONOMIC, POLITICAL, AND LEGAL TRANSFORMATION 112 (Mark Dawson et al. eds., 2015).

[50] *See* cases cited *supra* notes 2–3.

[51] *See, e.g.*, Case C-226/13, Fahnenbrock and Others v. Hellenic Republic, ECLI:EU:C:2015:383.

[52] *See* Karl-Heinz Ladeur, *The Postmodern Condition of Law and Societal "Management of Rules": Facts and Norms Revisited*, 27 ZEITSCHRIFT FÜR RECHTSSOZIOLOGIE 87 (2006); THOMAS VESTING, RECHTSTHEORIE 113–15 (2d ed. 2015).

[53] *See* ULRICH BECK, RISK SOCIETY: TOWARDS A NEW MODERNITY (Mark Ritter trans., Sage 1992) (1986); FRANÇOIS EWALD, L'ÉTAT PROVIDENCE (1986).

[54] *See* Philippe C. Schmitter, *Still the Century of Corporatism?*, 36 REV. POL. 85 (1974); Ernst-Hasso Ritter, *Der kooperative Staat: Bemerkungen zum Verhältnis von Staat und Wirtschaft*, 104 ARCHIV DES ÖFFENTLICHEN RECHTS 389 (1979).

https://doi.org/10.1017/S2071832200021441 Published online by Cambridge University Press

of a risk to the financial stability of the euro area, the sustainability of public debt, and the actual or potential financial needs of a member state to the experts of the European Commission, the ECB, and the IMF.[55] Furthermore, Article 13(7) of the ESM Treaty entrusts the same institutions with monitoring compliance with the conditionality attached to the financial assistance facilities granted to ESM member states.[56] Even the courts heavily rely on economic knowledge when reviewing the legal constructions that aim at restructuring sovereign debt in the euro area. Thus, the German Federal Constitutional Court (FCC) heard representatives of the ECB and the German Bundesbank as expert third parties pursuant to Section 27a of the FCC Act in its proceedings on the constitutional complaint against the establishment of the ESM.[57]

The extensive recourse to the law during the current euro crisis may be animated by a firmly held belief in its previous capacity for achievement. At the same time, new tools of legal regulation and judicial control attest a remarkable assertiveness of the law in this context. Nevertheless, the law will inevitably lose relevance to the extent that it cedes to economic imperatives.

D. Function

As the euro crisis impairs both the performance and the relevance of the law, the question arises of whether the law itself will have to change in order to hold its position in contemporary society. Indeed, Luhmann supposed that a total decline of the law in the evolution of world society was highly improbable because a one-sided reliance of society on cognitive mechanisms of processing disappointments would foreclose any confident orientation and bring with it unbearably high risks.[58] Yet he contemplated that the law would perhaps have to take into account the fact that the emerging world society gives primacy to a cognitive style of orientation. Such a transformation would then imply "the inclusion of cognitive mechanisms in the essentially normative structure of law."[59]

In the most extreme case, the genuine function of the law—the counterfactual stabilization of normative expectations—would be affected by such a transformation. As Luhmann proposed:

[55] *See* ESM art. 13(1).

[56] *Id.* art. 13(7).

[57] *See* Bundesverfassungsgericht [BVerfG] [Federal Constitutional Court], Mar. 18, 2014, 135 ENTSCHEIDUNGEN DES BUNDESVERFASSUNGSGERICHTS [BVERFGE] 317, 371.

[58] *See* LUHMANN, A SOCIOLOGICAL THEORY OF LAW, *supra* note 8, at 262.

[59] *Id.*

https://doi.org/10.1017/S2071832200021441 Published online by Cambridge University Press

> Law would take the form of normed models of behaviour which have been drafted as solutions to recognised problems, are legislated upon, tried and changed according to the rules of experience. Normativity would then only have the function of securing the constancy of expectation as long and in as far as it appears meaningful. Moral and ideological reasoning would then be replaced by a functional critique.[60]

As a matter of fact, this description accurately captures the features of the supranational and international instruments that aim to restructure sovereign debt in the euro area. The legal measures adopted to safeguard the financial stability of the euro area are constantly revised, amended, or complemented as soon as it turns out that changed economic or other social circumstances compromise their goals. For example, after a second financial assistance program had expired, Greece immediately requested further stability support so that the third program was launched under the ESM in 2015.[61]

To be sure, the alterability of the law necessarily follows from its positivization. As Luhmann stated: "Positivity involves precisely the built-in capacity for learning in law despite its contradiction to the basic normative attitude."[62] Moreover, the advent of democracy has considerably enhanced the capacities for altering the law. For Luhmann, it seemed not even "too far-fetched to say that democracy is a consequence of the positivization of law and the ensuing possibilities of changing the law at any time."[63]

Yet, with regard to the supranational and international instruments that aim to restructure sovereign debt in the euro area, the inclusion of cognitive mechanisms in the normative structure of the law reaches a new dimension that was unknown before. On the one hand, economic imperatives determine the law. On the other hand, fast-changing social circumstances require constant adaptations of the law. Meanwhile, the courts grant a large degree of leeway in regulating the euro crisis to political experiments, if only not to compromise the project of European integration as a whole. For example, the German FCC

---

[60] *Id.* at 264.

[61] *See* Financial Assistance Facility Agreement Between European Stability Mechanism and the Hellenic Republic and the Bank of Greece and Hellenic Financial Stability Fund, EUR. COMM'N (Aug. 19, 2015), http://ec.europa.eu/economy_finance/assistance_eu_ms/greek_loan_facility/index_en.htm.

[62] LUHMANN, A SOCIOLOGICAL THEORY OF LAW, *supra* note 8, at 262.

[63] LUHMANN, LAW AS A SOCIAL SYSTEM, *supra* note 8, at 404.

https://doi.org/10.1017/S2071832200021441 Published online by Cambridge University Press

finally approved the OMT program of the ECB,[64] even though it had initially expressed strong constitutional objections and submitted its first request for a preliminary ruling to the ECJ.[65] Taken together, these developments cause concern that the law might soon forfeit its normative character entirely in the face of the euro crisis. Under such circumstances, it can no longer adequately fulfill its function to counterfactually secure expectations.

Unfortunately, legal scholarship does not offer much guidance here either. It is largely at loss with assigning a proper role to the law in respect of financial crisis. So far, it has neither carved out any particular contribution that the law could make in taming financial crisis, nor does it more generally reflect on how to regain the autonomy of the law against the pull of economics. On the contrary, many scholars who are interested in law and finance do not pursue genuinely juridical interests. Some of them manifestly explore economic issues with economic methods.[66] Others limit themselves to describing and analyzing the various instruments of financial market regulation.[67] Even some more ambitious legal theories of finance turn out to be predominantly empirical observations on the role of law in the financial system.[68] While much has been gained from this scholarship, legal theory is now confronted with the pressing task of developing a specifically legal epistemology that provides some guidance about how the law is to deal with extra-legal, especially economic, knowledge.[69]

E. Legitimacy

The view from systems theory may finally cast a glance on the normative issues of sovereign debt structuring in the euro area, notably the question of legitimacy. As a sociological position, it may not submit a normative proposal in its own right. It may, however, offer a tentative outlook on the fate of democracy in the current stage of European integration.

---

[64] *See* Bundesverfassungsgericht [BVerfG] [Federal Constitutional Court], June 21, 2016, Case No. 2 BvR 2728/13 et al., http://www.bverfg.de/e/rs20160621_2bvr272813.html.

[65] *See* Bundesverfassungsgericht [BVerfG] [Federal Constitutional Court], Jan. 14, 2014, 134 ENTSCHEIDUNGEN DES BUNDESVERFASSUNGSGERICHTS [BVERFGE] 366.

[66] *See, e.g.*, EMILIOS AVGOULEAS, GOVERNANCE OF GLOBAL FINANCIAL MARKETS: THE LAW, THE ECONOMICS, THE POLITICS (2012).

[67] *See, e.g.*, NIAMH MOLONEY, EU SECURITIES AND FINANCIAL MARKETS REGULATION (3d ed. 2014).

[68] *See* Katharina Pistor, *A Legal Theory of Finance*, 41 J. COMP. ECON. 315 (2013).

[69] *See* Ino Augsberg, *Some Realism About New Legal Realism: What's New, What's Legal, What's Real?*, 28 LEIDEN J. INT'L L. 457 (2015); *see also* ECONOMIC METHODS FOR LAWYERS (Emanuel V. Towfigh & Niels Petersen eds., 2015).

https://doi.org/10.1017/S2071832200021441 Published online by Cambridge University Press

Many commentators regard the current attempt at restructuring sovereign debt in the euro area as undemocratic and, hence, illegitimate. In their view, the various supranational and international instruments aimed at ensuring the stability of the euro are elitist constructions, created by executives and implemented by experts, while evading participation and control by both European and national parliaments.[70]

In contrast, the sociological appraisal may—irrespective of its findings on efficiency—juxtapose a more favorable reading of the continuing political negotiations about how to cope with the euro crisis that ultimately result in the formation of supranational and international law. Indeed, it does not appear erroneous to think that the processes of mutual observation, recognition, and contestation among the various constituencies involved, including representatives of governments, institutions of the EU, central banks, national parliaments and peoples via referenda, as well as European and national courts, bring about a new kind of transnational democracy.[71] It may also be possible to detect a variant of the separation of powers here.[72] In such a setting, democratic rule is not grounded on hierarchical chains of legitimacy and representation. Instead, the heterarchical processes of mutual observation, recognition, and contestation among the various constituencies involved serve as a substitute for the lack of elections and parliamentary decision-making.[73] As some proponents of systems theory assert:

> A non-hierarchical variant of democracy would focus less on common decision through sovereign organized unity of will than on producing a distributed self-observation and observation of others made possible by a "network of networks" and the associated productive association possibilities and constraints,

[70] *See, e.g.*, Fritz W. Scharpf, *Monetary Union, Fiscal Crisis and the Pre-Emption of Democracy*, 9 J. COMP. GOV'T & EUR. POL'Y 163 (2011); Nicole Scicluna, *Politicization Without Democratization: How the Eurozone Crisis Is Transforming EU Law and Politics*, 12 INT'L J. CONST. L. 545 (2014); Christian Joerges, *Europe's Legitimacy in the Crisis*, *in* BEYOND THE CRISIS: THE GOVERNANCE OF EUROPE'S ECONOMIC, POLITICAL, AND LEGAL TRANSFORMATION 167 (Mark Dawson et al. eds., 2015).

[71] *See also* Goldmann & Steininger, *supra* note 6.

[72] In a different context, *see* Anne Peters, *The Globalization of State Constitutions*, *in* NEW PERSPECTIVES ON THE DIVIDE BETWEEN NATIONAL AND INTERNATIONAL LAW 251, 273 (Janne Nijman & André Nollkaemper eds., 2007).

[73] For a related concept of democracy within the nation-state, *see* PIERRE ROSANVALLON, COUNTER-DEMOCRACY: POLITICS IN AN AGE OF DISTRUST (Arthur Goldhammer trans., Cambridge University Press 2008) (2006). For some applications to international law, *see* NICO KRISCH, BEYOND CONSTITUTIONALISM: THE PLURALIST STRUCTURE OF POSTNATIONAL LAW 264–76 (2010); Isabelle Ley, *Opposition in International Law: Alternativity and Revisibility as Elements of a Legitimacy Concept for Public International Law*, 28 LEIDEN J. INT'L L. 717 (2015).

https://doi.org/10.1017/S2071832200021441 Published online by Cambridge University Press

> which are so openly dimensioned that far-reaching inclusion of citizens is guaranteed.[74]

It should be noted, however, that this vision of democracy does not include an apology of the status quo of European integration. In no way does it take side with keeping the euro area as it currently stands. On the contrary, continuing contestation on either plane may ultimately provoke or require a "Grexit," for example.

Yet an equivalent of democracy that deserves its name presupposes that choices can freely be made and that alternative avenues are available. Whether these conditions are currently met in the EU may be doubted on good grounds. For some constituencies, a voluntary decision is frustrated by the constraints of economic hardship. For others, it is corrupted by the path dependency of the prior political decision to introduce the euro as a single currency.

[74] Karl-Heinz Ladeur, *Globalization and the Conversion of Democracy to Polycentric Networks: Can Democracy Survive the End of the Nation-State?*, *in* PUBLIC GOVERNANCE IN THE AGE OF GLOBALIZATION 89, 113 (Karl-Heinz Ladeur ed., 2004).

https://doi.org/10.1017/S2071832200021441 Published online by Cambridge University Press