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Introduction: Law, Legitimacy, and Crisis Government

Consider the following three descriptions of government responses to the financial crisis:

—Because they wanted access to money without having to get the legislature’s approval, government officials interpreted an old statute in a fairly far-fetched way to commit up to \$50 billion to guarantee that private investors would bear no risk of losses.

—Pursuant to the terms of a law just passed, the government offered banks an investment of capital at fairly favorable terms.

—The government left undisturbed several contracts between a private firm and its employees, concluding that it was legally obligated to do so.

From these descriptions, you might naturally imagine that outside observers would be outraged at the first action for its twisting of the law and accepting of the second and third for their clear compliance. After all, respect for the rule of law is one of the hallmarks of our system of government.

You would be very wrong. The first action described, through which the Treasury Department made a crucial intervention to support the money market industry at the peak of the financial crisis in September 2008, occasioned almost no criticism at the time and has quickly receded into historical memory. The second action, which was the first major use of the crisis-inspired Emergency Economic Stabilization Act (EESA, better known as TARP) passed in October 2008, received scathing criticism both from those who felt the government was effectively running roughshod over private firms’ rights and from those who felt that the particular nature of the action was an inappropriate use of the resources

allocated by the law. Years later, neither group of critics has been much mollified; angry accusations of Godfather-style extortion and bait-and-switch deception persist, if at a lower volume. The third action, in which the government decided in March 2009 that it could take no legally valid action to stop bonus payments to employees at the mostly government-owned insurance giant AIG, inspired the most fearsome public outcry of the whole crisis. A public whose sense of fairness was deeply offended was profoundly unmoved by professions of legal limitations—though, as it turned out, elected officials were somewhat more sensitive to what the law required, ultimately leading them to step away from the most legally problematic actions under consideration.

This book attempts to shed light on this divergence between legality and legitimacy during crises. It does so by offering a comprehensive account of the government's responses to the financial crisis of 2008 and the political and legal controversies that surrounded them. Throughout, it attempts to accurately describe how the public reacted to each action and analyze why certain issues aroused so much more anger than others.

As with any exploration of recent history, the events described still inspire strong and conflicting feelings. Their place in history is in the early stages of being determined, and so partisans of various interpretations are likely to denounce those who fail to ratify their own views. In the case of the recent crisis, two polar extreme views are now vying for contention. For some, it is all but self-evident that what the government did during the crisis was outrageous and that the so-called bailouts were a fundamental betrayal of the public trust as well as a perversion of both statutory and constitutional law. At the other end of the spectrum, some will profess astonishment at the idea that the government's actions deserve further scrutiny, either in a legal or political sense. They believe everything that the government did was perfectly above board and that it is downright petty to quibble over insubstantial legal trifles at this point in time, especially given how well these programs turned out to perform.

There is little purpose in coyly hiding my own views. As the crisis unfolded in 2008 and 2009, much of what the government was doing struck me as legally unjustifiable and worrying. I was skeptical that "loans" would ever be paid back, or even that the policymakers involved believed that they would be; as a result, many of the government's actions struck me as illicit forms of spending. As those loans were paid back at levels that showed my initial thinking was mistaken, and as I learned more about the details of the responses and the history of other crisis responses, I became considerably less distressed, and more convinced that discretion ought to be welcomed, at least in limited circumstances. There are many choices that remain troubling to me, and my

judgments are sure to be evident throughout the book. But the main purpose of the book is not to simply argue for a particular judgment about each of the various crisis responses. Convincing either of the two types of critics noted above of the merits of my judgments is not my priority.

Instead, my aim is to illuminate for readers of all perspectives some of the dynamics of establishing legitimacy during a financial crisis, especially the role of law in that process. Responding to crises—whether military or financial—raises several dilemmas for a country's leaders. Relying on already existing legal authorities may be insufficient to meet the challenges, and exigency may make obtaining new ones impossible. History generally esteems leaders who seize these moments and respond forcefully, whether in strict compliance with the law or not.

Some scholars thus conclude that legal constraints have come to play almost no role in shaping the legitimacy of responses to crisis, but I reject that view.¹ Especially when leaders enjoy little public trust, bold crisis actions may be regarded as illegitimate if they flaunt the law. Although it is easy to overestimate the importance of the rule of law in crises, complying with the law remains one important factor for legitimacy. And achieving legitimacy is often a necessary prerequisite to successfully responding to a crisis.

I argue that legality is neither necessary nor sufficient to establish an action's legitimacy during a crisis. If "it's against the law" is the only argument against an action, then this legalistic point will be little impediment to establishing legitimacy. From the other direction, if an action lacks legitimacy for various reasons, declaring that it is consistent with the law (or even legally mandatory) will not always confer legitimacy on it. Indeed, I argue that there is no single factor that can reliably secure legitimacy for a crisis response. Obedience to established law, democratic support, trust in crisis leaders, and a widespread sense that those leaders will be held accountable for any abuses will all contribute to legitimacy, but none of these factors is indispensable. Looking to the future, I recommend both a greater investment in clear legal limitations and a realistic acceptance of law's limitations as embodied by a limited but substantial discretionary fund to be used at the executive branch's disposal to combat financial crises.

To begin to explain these claims, the concept of legitimacy I employ demands some clarification at the outset.

What Is Legitimacy?

There are two ways of thinking about legitimacy: normatively or as a positive social fact. Academic political theorists and armchair moralists alike most often engage in the normative enterprise: developing standards of legitimacy

that government actions must meet and evaluating particular actions with regard to these standards. (Lawyers focus on the somewhat unusual normative standard of legality, to which I return shortly.) To anyone who has ever argued about the legitimacy of government actions in normative terms, it should be obvious that judgments about legitimacy are often sharply conflicting. This is true even when discussions clearly distinguish between “actions that are legitimate” and “actions that I approve of,” which many do not.

Treating legitimacy as a social fact, as I do in this book, is somewhat more conceptually difficult. Following Max Weber’s empirical approach, this approach does not deny normativity but says that the social scientist interested in legitimacy ought to understand its emergence as it happens, rather than as the practitioners of “legal dogmatics” say it ought to.²

In a sense, legitimacy as a social fact can be understood as the aggregate product of all of the normative arguments—including arguments that never actually happen and that people perhaps are not even prepared to have. That statement requires some unpacking.

Legitimacy as a social fact is necessarily a collective phenomenon. If every person were an independent-minded political theorist and a perfect observer of every government action, then political legitimacy writ large could probably be fairly characterized as an aggregated sum of all citizens’ judgments about legitimacy.³ As long as time and attention are scarce, however, a real citizenry can never approach this (rather dystopian-sounding) ideal. Rather, certain shared ideas about legitimacy shape widespread perceptions, both because citizens apply them in similar ways and because elite opinion leaders apply them and have others adopt their judgments as authoritative. This application of ideas to particular instances is hardly ever a matter of applying well-defined logic, though. Instead, opinion at every level of engagement is shaped by a contest of rhetorical framings, selective attention to facts, and group affinity; opinion leaders seeking audiences for their own views about legitimacy are sensitive to which arguments gain currency and thus are also followers of broad sensibilities.

Legitimacy for the whole polity is thus an emergent and path-dependent phenomenon, characterized by dozens of feedback mechanisms that involve those who develop criticisms, those who rebut them, and those who determine their own judgments about these debates and determine their own level of engagement with them. Predicting social legitimacy in advance is generally a fool’s errand, as so much depends on how arguments play out in real time; that said, it is far from random, and there are characteristics of actions that usually contribute or detract from their legitimacy in predictable ways. These

characteristics correspond to normative conceptions of legitimacy held by many people—but I must emphasize that I do not prejudge whether people will actually apply those factors in every case (let alone whether they should). Indeed, one of the book's contributions is to show how missing certain legitimating factors often thought of as absolutely crucial—including legality—can turn out not to create legitimacy problems.

By studying at what points a lack of legitimacy produced political strife during the recent crisis, I draw useful lessons about what policymakers can do to improve the legitimacy of their future actions. But I have no illusion that these lessons will be anything other than helpful heuristics: probabilistically useful but by no means a recipe for certain success.⁴ Politics, in its most universal sense, is about determining what collective actions are legitimate, and nobody should imagine that it can be reduced to a simple science—it is, after all, properly thought of as the art of the possible.

That I offer no scientifically rigorous way of ascertaining legitimacy after the fact will undoubtedly worry those who crave certainty. In part to satisfy such worries, I frequently make use of public opinion data obtained through polling, and it can often provide a useful indicator. But the questions asked by pollsters are generally too vague and haphazardly deployed to give a clear sense of reactions to specific policies; and even if I had been able to conduct my own polls consistently, I would not argue that legitimacy is equivalent to public opinion. This is because polling obscures the huge variations in the intensity of people's investments in understanding political developments. This is well understood, but little dwelt upon, by students of political behavior, who nevertheless often confine themselves to the kinds of questions that polling data are able to speak to more or less adequately.⁵

In studying the debates surrounding the responses to the financial crisis, it is important to emphasize several facts that are rarely acknowledged, perhaps because doing so seems unscholarly: that it is difficult, time consuming, confusing, and often boring to penetrate the mass of information about these complicated events. This is true even for those of us who invest large parts of our lives poring over particulars. (Indeed, there are a few matters that probably deserve treatment in this book but managed to evade coverage because of their technical slipperiness.)⁶ Treating these features of our political life as merely incidental unnecessarily renders scholarly discussions less realistic.

This book frankly acknowledges that lack of attention and ignorance are the defining features of most people's relationship to particular governmental actions. These actions' legitimacy will be a function of the interaction of underlying attitudes about government with (generally unfocused) exposure to

the playing out of arguments among a small elite. The most common underlying attitudes are blanket cynicism, blanket trust (quite uncommon today), and blanket indifference, each of which has the power to wipe out the impact of any debate. More consequential for determining society-wide legitimacy are those people more able to adjust their judgments about a policy's legitimacy in response to ongoing elite debates, at least some of the time, and therefore to vary their levels of "specific support" from one policy action to another.⁷ The relevant elite is one of knowledge and opinion; especially in the age of the Internet, it is open to those who decide to invest their time and energy—at least in part. Our national conversations are still disproportionately centered in a few newspapers, and those who have access to the opinion pages of the *New York Times* and the *Wall Street Journal* have greater ability than the rest of us to affect judgments about legitimacy.

To make this at least a little more concrete: The median citizen, or even the median voter, probably understands little about the role played by the Treasury or the Federal Reserve in responding to the financial crisis. The median engaged citizen has never heard of Maiden Lane LLC, let alone pondered its legal justification. Even the median member of Congress must find a great deal about the government's response to the crisis quite obscure. Policies such as "the auto bailouts" are far more widely opined about—although many of those most willing to stake out a position on the legitimacy of a policy like that one, the politics of which ended up polarized along partisan lines, may be unable to say with any specificity what the intervention consisted of. But it would be wrong to infer that there is no *there* there when it comes to determining legitimacy: as chapter 5 shows, the contentious debates among experts about the legitimacy of the Chrysler bankruptcy are extremely substantive and illuminating, and the hard-hitting legal criticisms offered at the elite level manifested themselves as a greater willingness among Republicans to pound the table about the issue.

Although not formally systematized, the book's approach to legitimacy nevertheless attempts to distinguish levels of critical reactions. Legitimacy is clearly not a binary variable, though it is sometimes discussed in that way. Instead, there is a spectrum, with actions inspiring violent revolution on one end and actions hailed with unanimous acclamation on the other. Intermediate cases are not so easily deemed to possess or lack legitimacy: if a substantial minority angrily complains that an action is illegitimate but is not angry or well mobilized enough to effectively oppose it; if most people raise their eyebrows when learning of an action but then reluctantly acquiesce; if a few people are upset by an action but most are not even aware of it. To place

different actions on this spectrum, I consult a variety of sources, gauging the intensity of the reaction among journalistic commentators, blogging academics, and angry commenters across the web. Activity in Congress is a crucial barometer: if an issue is never raised by some legislator hoping to make a name for himself through hard-hitting oversight, it probably failed to make much of an impression on the broader public. If it inspires table-pounding hearings or the introduction or even passage of bills, then worries about legitimacy were more consequential.

My own judgments about levels of legitimacy are certainly contestable, but I have no axe to grind on this score; nothing in this book is meant to reveal to readers an elegant theoretical relationship between certain characteristics of government action and legitimacy.⁸ Instead, I offer four closely intertwined legitimating factors, each of which can be expected to contribute to or detract from legitimacy: legality, democratic legitimacy, trust, and accountability. I briefly introduce these factors here and go on to explore how they are implicated during crises in chapter 2.

Four Legitimizing Factors

The first, and often most important, factor in determining a government action's legitimacy is its legality. For an action to be legitimized as legal, it must have a valid legal pedigree. That is, it must be authorized by a law that itself originates from a widely accepted source of law.

Where this deep acceptance comes from is a difficult question in its own right and has inspired a great many valuable treatises in the philosophy of law, but I largely put such questions aside.⁹ In the contemporary United States, the accepted root source is generally the constitution of a state or of the federal government, and in political practice this does not occasion much controversy.

Instead, disagreements are rooted in the fact that the Constitution and the manifold statutes passed under its auspices are ambiguous, and so it is often difficult to say with certainty whether an action is legal. Those who carry out the action are almost certain to insist that they have legal sanction, but this does not make it so. Neither is a critic's insistence that an action is unsupported by law proof of anything. Laws are not self-interpreting, which means that the practical constraining force of statutory provisions will depend in large part on whether the initial interpretation can be contested and remedied, usually in court.¹⁰ This can be especially consequential if the executive branch is willing to furnish creative, expansive statutory interpretations of existing statutes to justify its conduct.¹¹ Courts, or a legislature refining

the scope of the law through amendment, can provide some clarity. But we should not expect courts to provide once-and-for-all answers that will be convincing to all parties. Rather, questions of legal compliance can acquire a political character, such that sometimes legality comes to be subject to adjudication by wider audiences.

Legality also has a process component: not only the substance of government actions but also the manner of their formulation is crucial to establishing legality. At least in the United States, with both constitutional guarantees of due process and Administrative Procedure Act guarantees of fair hearings, if an action is improperly generated it may well be illegal. Such attention to process is at the heart of what is usually called the rule of law (which is examined more closely in chapter 2). Government actions will lack legal process legitimacy if they seem to be generated by the caprice of government officials rather than through reasoned, publicly justifiable modes of decisionmaking. Such a failure signifies more than a breach of legal etiquette: there is an expectation that the discipline of reason-giving promotes more-just outcomes.¹² If, in reviewing government actions, courts fail to protect these deeper values and become thought of as mere rubber stamps for government actions, allowing executive branch officials to do whatever they please, then legal process will no longer confer legitimacy.

The second legitimating factor, democratic legitimacy, often flows naturally from legality. Widespread agreement on the propriety of an action—or pervasive indifference about it—should mean that its democratic *bona fides* can be solidly established by linking it to a law passed by duly elected legislators, who are thought to represent the popular will well enough. Even when there is more dissent, this process often works smoothly: representative legislatures are supposed to meaningfully deliberate about a topic, virtually represent the interests of all of the country's people, and produce a compromise that can be accepted as the fruit of a well-established process. The legislature can thus act as the key legitimating organ of government.

But compliance with legality might fail to produce democratic legitimacy for several reasons. First, the legislators themselves might lose voters' confidence as a representative body. If large portions of the public believe legislators to be corrupted or unrepresentative of their interests, they will have no reason to accept the outcomes of the latter's deliberations as legitimate.¹³ Second, even if the legislature generally retains some confidence, some of its actions might be derided as abominations of process. If many citizens have the sense that some legal change was effected by circumventing required processes through parliamentary trickery, then it may be seen as tainted fruit—legal in

the sense of being on the law books but nevertheless illegitimate with reference to democratic values.¹⁴ If the system is perceived as hijacked, its official sanctioning will be worth little.

Finally, and most important, nothing can effectively force a democratic public to treat actions produced even by immaculate processes as legitimate. In some instances, people disregard legal formalities and instead judge an action's legitimacy far more directly. Even with perfect legal pedigrees, some actions may be rejected as abhorrent. Just as important, some crisis actions without proper legal justification may nevertheless be accepted as legitimate. If a society faces an existential threat, actions taken in response may strike people as inherently legitimate, no matter how precipitate. To give two of the clearest examples, defensive war tends to strike people as inherently legitimate, as does the practice of instituting severely coercive quarantines in response to the emergence of deadly outbreaks of disease.¹⁵ Because they understand this reaction to claims of necessity, leaders have incentives to overstate the seriousness of emergencies or even invent them—which means that their ability to gain democratic legitimacy through such appeals will depend on their credibility with the public.

That brings us to the third legitimating factor: trust. When citizens put their faith in the particular persons holding offices rather than simply depend on institutional mechanisms, it does not necessarily mean the “rule of men”—although in its starkest form, in which a polity submits to what Weber calls “charismatic authority,” it could.¹⁶ Far short of that, trusted officeholders can be given limited discretion to wield state power on behalf of the common good. Because the necessary trust depends on belief in both the possibility and existence of public-spiritedness, cynicism about the nature of politics owing to a perception that leaders have been corrupted erodes trust-based legitimacy.

Many modern liberal thinkers, especially those of a legalistic bent, have argued that trusting in the goodness of our leaders and therefore leaving them unfettered by legal constraints has no place in the American variety of the rule of law. James Madison's famous prescription in *Federalist* No. 51, that men not being angels, “ambition must be made to counteract ambition,” certainly represents a skeptical stance.¹⁷ But while distrust of those in power certainly has deep roots in American political thought, the attempt to entirely expel the need for trust overstates things and actually represents a significant departure from the classical liberal tradition, which emphasized residual prerogative powers.

As Clement Fatovic describes, modern Western political thought traditionally recognized what Machiavelli called *fortuna*: the idea that contingency is

the one constant in politics. In response, political theorists usually saw the need to rely, at least in part, on energetic and virtuous executives who could respond to emergencies as they arose. The more trust the leader merited, in this view, the greater the scope of the allowable discretion and the greater the polity's capacity to meet the challenges of fortuna. Far from denying this fact, classical liberal theorists including Locke, Hume, Blackstone, and the American framers all believed there was a place for an executive prerogative power within a well-functioning state that would complement, rather than threaten, the rule of law that controlled during normal circumstances.¹⁸ Locke's chapter on prerogative in his *Second Treatise* may seem jarring to those who think of him as the champion of a constrained sovereign, but it admits quite an expansive prerogative:

This power, whilst employed for the benefit of the community, and suitably to the trust and ends of the government, is undoubted prerogative, and never is questioned: for the people are very seldom or never scrupulous or nice in the point; they are far from examining prerogative, whilst it is in any tolerable degree employed for the use it was meant, that is, for the good of the people, and not manifestly against it: but if there comes to be a question between the executive power and the people, about a thing claimed as a prerogative; the tendency of the exercise of such prerogative to the good or hurt of the people, will easily decide that question.¹⁹

For Locke, trust in the sovereign is the key variable: for a leader who has the people's trust, power to act apart from the law on behalf of the common good not only should be expansive but as a sociological fact will be expansive.

For the authors of *The Federalist Papers*, trust plays a far more important role than Madison's No. 51 suggests. This is, in the first place, a function of the circumstances under which the Constitution emerged: not having been charged specifically with offering a new charter of government, Madison in *Federalist* No. 40 defends the need to advance collective interests through changes "instituted by some *informal and unauthorized propositions*, made by some patriotic and respectable citizen or number of citizens."²⁰ In Alexander Hamilton's brief for "energy in the executive" in *Federalist* No. 70, he offers that "the ingredients which constitute safety in the republican sense are a due dependence on the people, and a due responsibility," implying a reciprocal trust between the people and their leaders.²¹ And in sparsely defining the responsibilities of the president, the framers were influenced considerably by the trust they had in the man they rightly assumed would be the first

occupant of that office, George Washington. Rather than supplanting the need for trust, institutional checks would complement the need for virtuous leaders, especially in the presidency.²²

The fourth and final legitimating factor is accountability. Recognizing that *ex ante* process constraints may not be able to fully legitimate government actions, legitimacy can be conferred by the willingness of officials to have their actions subjected to *ex post* scrutiny and themselves to some kind of ultimate accountability. Accountability legitimacy suffers if citizens sense that officials act with *de jure* or *de facto* impunity, such that they may be thought of as above the law and unanswerable to politics.

Using accountability mechanisms to produce legitimacy is a natural substitute when trust is in short supply, as embodied in the maxim that Ronald Reagan made famous: “Trust, but verify.” *Ex post* accountability can take either legal or political forms. Legally, it may include personal liability for officials if they have used their positions of authority to pursue illegitimate ends—though “illegitimate” here clearly begs the question. Politically, it may include oversight hearings and reviews designed to elicit facts that were obscure to the public as actions were being taken, thus allowing citizens to make good use of their democratic control in the future. To the extent a government official actively courts responsibility, by some form of the declaration that “the buck stops here,” and presents himself or herself as accountable, this may lend legitimacy.

Perhaps paradoxically, being more accountable can thus make a government official or institution more powerful. If citizens know that actions will ultimately be minutely scrutinized, they will extend greater trust as they are taken, even if the actions seem problematic. This accountability can be self-produced by the government, but it can also come from external sources. As I show in chapters 2 and 6, the existence of a “synopticon” made up of both government inspectors general and private reporters, lawyers, and others enables the government to be more assertive than it might otherwise be.

Identifying these four factors that contribute to legitimacy is not meant to provide some sort of unassailable taxonomy of how things really are in the world, such that one action is legitimated under one category and requires proper categorization. There is clearly overlap between them, and different categorizations can be easily proposed.²³ But if legitimacy remains a slippery phenomenon, this should not deter our study of it. Our government’s ability to respond to crises in ways the public regards as legitimate is among the most important aspects of our political system, one that may well determine its very ability to survive. While making judgments about what actually produces legitimacy is difficult, it is not impossible, and the difficulty must be met head

on. Even if we cannot hope to arrive at a single dependable recipe for achieving legitimacy in normal times or in crises, examination of the ways in which particular government actions affected legitimacy can give us insights into the how and why of legitimation.

Why Does Legitimacy Matter?

Why does all this matter? Americans in the post–cold war world sometimes have a difficult time believing that our current system of government could meet any fate other than perpetual motion, but this is a dangerously complacent illusion. More than at any time in the past quarter century, we are beginning to hear murmurings about exhaustion of American government and the relative inferiority of our constitutional system. These impressions are fueled in large part by discontent with the responses to the financial crisis.

This is not a wholly novel situation for the country. As Ira Katznelson argues in *Fear Itself*, the struggle to legitimate America’s system of government was the overarching theme of politics in the 1930s, and the success of these efforts was not at all a foregone conclusion. Indeed, conducting the nation’s affairs against the backdrop of widespread disaffection forced America’s leaders into several troubling compromises and alliances that left an unfortunate legacy.²⁴ Many of the conditions that made the 1930s such a perilous decade for democracy in America and in Europe seem remote today, but the comparison is not one that should be shrugged off lightly. Our form of government’s ability to secure legitimacy over the past seventy-five years has been one of its greatest assets, but it should not be thought of as a permanent quality of American life incapable of being squandered. Rejection of our form of government is far from imminent, but neither is it unthinkable.²⁵ Even if the country manages to steer well clear of governmental collapse, diminished legitimacy can potentially handicap what a government is able to accomplish. As James Gibson puts it, legitimacy “is a reservoir of good-will that allows the institutions of government to go against what people may want at the moment without suffering debilitating consequences” and thus one of the most important enablers of long-term thinking in moments of calm and crisis alike.²⁶

In spite of its obvious importance, the process of legitimation in many modern democracies, and certainly our own, is quite haphazard and uncertain. It is too often an afterthought for government officials who imagine they have a kind of Rooseveltian mandate that they actually lack and who do not think of maintaining and improving the government’s legitimacy as their own responsibility. Government lawyers attempt to ensure that their clients do not

make choices blatantly at odds with the law, but as this book explores, this effort is often insufficient to deliver legitimacy, especially in a crisis. Political advisers, and political principals themselves, can and must think about legitimacy, but they consider it alongside what seem like far more pressing questions of what policies will be effective at advancing their underlying political aims—that is, what should be done.

Many readers—especially those who have worked on crisis responses from within government—may think that there is not much to be gained by separating legitimacy from efficacy, as efficacy is the most important determinant of legitimacy. (This is the view advanced by former Treasury secretary Timothy Geithner, discussed in chapter 5.) That is too simplistic, even if it is often right.

A government's legitimacy undoubtedly has more to do with the overall conditions in the country than any other factor: surely the best thing 2008 crisis fighters could have done for our system's long-term legitimacy was to successfully overcome crisis and return the nation to economic growth. Throughout the book there is extensive discussion of the trade-offs that may exist between choosing efficacious actions likely to improve overall conditions—and thus improve legitimacy in the long run—and choosing actions likely to produce worse overall outcomes but achieve greater legitimacy in the short run.

But some steps can be taken to improve specific actions' legitimacy and the legitimacy of a whole crisis response strategy. Keeping in mind the risks posed by diminished legitimacy, policymakers should be far more attentive to achieving legitimacy for their policies than they were in the crisis.

Nor are legitimacy and efficacy always in tension; indeed, just as often, a government can't have one without the other. Both at the government-wide level and at the level of specific policies, a lack of legitimacy can impede effective action. Policies that lack legitimacy are more likely to be implemented half-heartedly or quickly reversed. A lack of legitimacy translates into a lack of dependability; especially in our system, policy is always contingent on politics. We can therefore see a reinforcing virtuous cycle—political legitimacy begets policy efficacy begets political legitimacy—or a downward spiral—policy failure destroys political legitimacy, making the possibility of future policy success more remote.

If any doubt the intrinsic importance of government legitimacy, then, its instrumental importance to effective government action ought to convince them that it is a subject worthy of attention.

One aim of this book is to make the consideration of legitimacy somewhat less haphazard by systematically considering how the crisis responses affect it.

My hope is that even if policymakers understandably do not make achieving legitimacy their primary objective, by taking the lessons of the recent crisis into account they will be able to more consciously improve the legitimacy of their future crisis actions.

The Limits of the Law

In shaping this advice, the book aims to convey a realistic sense of what the law can do to determine crisis actions and provide crisis legitimacy. For both purposes, legal and political commentators have a tendency to overstate law's powers.

First, although many speak of law as if it provides the entire basis for government action, law does not and cannot control all of the actions taken by government officials. This is in part because of limitations in legislative foresight and drafting ability and in part the consequence of intentional decisions to endow the executive branch with discretionary power capable of responding prudently to new conditions. Both the unintentional and conscious limitations of law are heightened in a crisis, when rapid reaction and creativity are at a premium. I argue that only unusually clear legal limitations provide dependable restrictions on government actions during crises—though I emphasize that there are indeed plenty of legal provisions that fit this bill.

I also highlight the way crisis conditions create space for meaningful exercises of power on the margins of legality—what I call “soft power.” As a crisis unfolds, top officials sometimes find they have the ability to steer the course of events by such subtle means as expressing their opinion, passing information from one party to another, convening meetings, and (somewhat less subtly) cajoling to encourage or opaquely threatening to discourage certain legal, private actions. Throughout the book, I take the inevitability of such “soft” actions for granted; anyone who proposes that officials will (or even should) entirely refrain from these behaviors merely because they do not straightforwardly emanate from legal commands is being naive—or, more likely, faux naive. That said, there is no question that exercises of soft power can easily shade into problematic coercion or even abuse of power. There is a fine line between suggesting that a course of action is likely to lead to bad results and further intimating that the state's (discretionary) legal powers will ensure those bad results. Offers are acceptable even when they create awkward choices; offers that can't be refused are presumably beyond the pale. But that line is difficult to discern clearly, and many of the responses to the financial crisis go to the edge of this boundary or beyond. On this score, I mostly preach

resignation: government officials are almost certain to use soft power in ways their friends see as boldly but righteously pushing the envelope and their adversaries see as crossing the line.

Soft power has historically been especially important in responding to financial crises. In the financial crisis of 1907—the second most serious of the twentieth century—it was the private magnate J. Pierpont Morgan who used his soft power most aggressively, hastily organizing the threatened financial trusts into a consortium patterned after regular banks' clearing houses and bullying and cajoling other financiers who were reluctant to put themselves at risk. Less important, President Theodore Roosevelt also used legally unanchored soft power to give Morgan the blessing of the White House.²⁷ Although many felt Morgan had beneficently acted as the savior of Wall Street, and by extension the nation's economy, it would be an understatement to say that he lacked the public's trust. And so while the actions of the rescue were based entirely on voluntary actions, they lacked legitimacy in the eyes of the broader American public. Congress held extensive hearings investigating possible improprieties and self-dealing, during which the possibility was raised that Wall Street had engineered the whole panic for its own gain.

But uses of soft power do not always create legitimacy problems. In 1998 Wall Street's health was threatened by the imminent demise of the much-celebrated hedge fund Long-Term Capital Management (LTCM). To overcome the coordination problem faced by the many firms that would be exposed to a chaotic failure of LTCM, the Federal Reserve stepped forward to act as a convener of the major investment banks. With the Fed's encouragement, fourteen banks worked out a rescue plan through which they would collectively infuse \$3.65 billion into the faltering firm and thereby avoid the fallout from having to unwind all of its trades. The Fed had been forced to use none of the heavy weapons in its legal arsenal, instead finding a way to effectively stave off a wide financial crisis wholly through soft power. Though many expressed worries that the Fed's actions created moral hazard by fostering the impression that it would step in to prevent any catastrophic failures, in general the legitimacy of the Fed's successful light-touch intervention was rarely questioned.²⁸

If law cannot be expected to provide the legitimating basis for every crisis response, its limitations are evident from the other direction too: especially in crises, obeying the law is no guarantee of legitimacy. The 1930s again provide an instructive example: as financial crisis and the Great Depression gripped the nation, legality had no more devoted servant than President Herbert Hoover, who famously believed in the power of voluntary private

action to combat the economic downturn. While he sometimes sought and secured limited legal changes to promote desired private investments (as with the Reconstruction Finance Corporation), Hoover mostly remained steadfastly devoted to keeping the federal government's role limited. Voters clearly signaled that course of action's lack of legitimacy in 1932 when they gave Hoover what remains the worst electoral defeat for any incumbent president in American history.

Hoover's successor, Franklin Roosevelt, struck a very different posture toward the law.²⁹ In his inaugural address, he declared that the nation's economic problems should be treated "as we would treat the emergency of a war,"³⁰ and he proceeded to go well past the edges of his office's normal legal powers in the manner of a wartime leader, declaring a national bank holiday on thin legal authority,³¹ devaluing the dollar against gold and then cavalierly setting its price over breakfast each morning,³² and frequently riding roughshod over normal legislative procedure as he extracted concessions of discretionary authority from Congress.³³ In his storied fireside chats Roosevelt deftly secured democratic legitimacy for these policies even when they obviously strained against the edges of the law. To this day there are many who would portray Roosevelt's actions as tyrannical, but from the start they have always been a distinct minority; three reelections and a lovely monument on the National Mall attest to Roosevelt's general stature. Hoover's name, meanwhile, retains its power as an epithet in American politics even after eighty years. When crises come, adherence to legality is no assurance of legitimacy; and aggressively pushing the boundaries of what is legal is no guarantee of illegitimacy.

Though none of its principal figures are likely to become as cherished as Roosevelt or as forsaken as Hoover, the recent financial crisis made the divergence of legitimacy and legality glaringly clear. As noted at the opening to this chapter, two of the actions that engendered the greatest outrage—the failure to rescue Lehman Brothers and the decision to honor AIG's preexisting bonus contracts—involved bowing to apparent legal limits. Perhaps justly, people apparently had the sense that if acting differently required bending the law, a truly committed group of crisis responders would have found a way to bend it. Conversely, the most aggressive legal maneuvers, such as the Treasury's guarantee of money market funds or the Fed's massive purchases of commercial paper, sometimes elicited barely a peep. I seek to explain the circumstances in which law will most successfully bind—not surprisingly, when it clearly sets the shape and outer limits of executive conduct—and to ponder how we can productively create space for decidedly unlawlike decisionmaking.

Plan of the Book

The book seeks to illuminate when and why legality and legitimacy split apart. It begins, in chapter 2, by giving fairly abstract consideration to this question. I consider how and why law and legitimacy may become competitors in crises and present different options for attending to legitimation during crises, including a resolute adherence to law, a derivation of expansive legal authorities “inherent” in the law, an abandonment of law in favor of plebiscitarian acclamation, and frank admission of extralegal action. Finally, I turn to the most common form of harmonizing law and legitimacy in modern times, the enabling act, in which a legislature transfers crisis policymaking powers to the executive branch while attempting to set temporal and substantive limits on the use of that power. I argue that courts have a difficult time enforcing any but the clearest limitations during crises, pushing legislatures to create alternative mechanisms to effectively hold accountable executives empowered by enabling acts.

The book then moves on to a detailed examination of the responses to the financial crisis of 2008. Chapter 3 covers events from mid-2007 through the climactic month of September 2008, showing how Ben Bernanke led the Federal Reserve to use its long-dormant crisis powers in unprecedented ways to limit the effects of the failure of Bear Stearns. I dub the seemingly unpredictable pattern of responses “adhocracy”: the government’s most important crisis responses flowed not from deliberation of lawmakers but from hurried decisions of unelected officials deriving their authorities from obscure sources.³⁴ An exception to this pattern was the response to the deterioration of the two giant government-sponsored enterprises, Fannie Mae and Freddie Mac, which flowed from legislation passed in July 2008. This example illustrates the limits of legislation in conferring legitimacy: simply being armed with recently passed legislation proved insufficient to clearly delimit the government’s response or to prevent serious challenges to the action’s legitimacy. September 2008 saw a brief resurgence in the importance (and hazards) of legal constraints with the fall of Lehman Brothers, and then a crescendo of adhocracy in the Fed’s rescue of AIG, the Treasury’s backstopping of money market funds, and a handful of other hastily arranged interventions. Once again, legality and legitimacy sharply diverged, with some of the crisis fighters’ most legally questionable decisions receiving the least scrutiny.

Congress finally took a central role in determining the shape of the crisis response when it passed the Emergency Economic Stabilization Act of 2008, better known as TARP, at the beginning of October 2008. Chapter 4 begins

with an extended look at the rancorous battle over that act. Contrary to many people's characterizations, Congress's deliberations were neither insubstantial nor fruitless: before acceding to Treasury secretary Henry Paulson's historic request for \$700 billion, they added several accountability mechanisms that would consequentially shape the political environment constraining the uses of the money. The chapter also shows how willing Congress was to allow the secretary to determine how these funds would be spent, flexibility that would be quickly used as the initial plan for asset purchases gave way to bank recapitalization. It then considers the accusations that TARP represented an illegitimate bait and switch. I also look at the way adhocism continued alongside TARP in the late Bush administration in the handling of the sales of Wachovia and Merrill Lynch, the creation of new Fed programs, a deepening of the commitment to support AIG, and the Federal Deposit Insurance Corporation-led creation of a universal bank guarantee. Finally, I examine how TARP was extended to the auto industry after Congress decided against passing auto-specific legislation in December 2008, in spite of the fact that this use of TARP went well beyond what the enabling act was intended to provide for. I argue that the commitment of administrations of both parties to the use of TARP for the auto industry limited the extent to which the basic legitimacy of that choice was questioned.

Chapter 5 follows the continuation of all of these crisis responses into the Obama administration. It examines the auto bailouts and bankruptcies, which inspired some of the bitterest legal confrontations of all the crisis responses. I show how claims of legality can be used to lend legitimacy to otherwise unpopular political decisions. The chapter considers the difficult balancing act between legality and legitimacy that the government faced in its role as a corporate shareholder, both in the case of General Motors and in the case of many banks. I also examine the legal disputes surrounding AIG and the government-sponsored enterprises, explaining how the legally motivated decision not to wipe out private shareholders of these rescued corporations eventually created dilemmas pitting legal requirements against the demands of legitimacy. I explain why judicial involvement (still ongoing) is likely to be relatively insignificant compared with political accountability mechanisms. A similar dynamic in the case of contractually obligated bonus payments at AIG led to the most heated showdown between law and legality in March 2009—with legality proving the victor in this case. The chapter then examines the distinctive elements of the Obama administration's strategy as laid out by Treasury secretary Timothy Geithner and the efficacy problems that a lack of legitimacy caused. I argue that the administration would have benefited from a

willingness to prioritize legitimacy, even when it might have conflicted with its beliefs about the surest way to fend off the financial crisis.

Chapter 6 revisits the years of crisis response through the lens of the various accountability mechanisms at work, including special bodies created by TARP such as the Special Inspector General for TARP and Congressional Oversight Panel as well as existing institutions such as the Government Accountability Office and the news media. It argues that by scrutinizing and criticizing the actions of the Fed and the Treasury these bodies helped to legitimize them in a backhanded manner: in spite of their best efforts, they never exposed any evidence of bad faith or self-dealing among the crisis fighters. Nevertheless, I consider the ways in which these agents of accountability also left lingering scars in the crisis fighters' legitimacy, with special attention to questions of the overall cost of the crisis responses and the accusations that the rescue of AIG was engineered as a "backdoor bailout" of Wall Street investment banks.

Chapter 7 offers concluding thoughts about where legality and legitimacy stand in the wake of the crisis. It examines the damaged legitimacy of the government's crisis responses, with special attention to two mass emanations of the nation's legitimacy concerns about the crisis response, the Tea Party and Occupy Wall Street movements, each of which channeled concerns about the legitimacy of crisis responses into demands for reform, especially of the Fed. I then look at how the Dodd-Frank Act enacted new legal constraints on future crisis responders, concluding that several of its alterations should be understood as a coherent prioritization of legitimation. I also take stock of the role that law played throughout the crisis, concluding that it is a mistake to discount it as irrelevant. Finally, I make several recommendations to help future crisis fighters better secure their legitimacy, including a stronger relationship with Congress, greater investment in making processes transparent and in educating the public about the nature of crisis responses, a greater willingness for Congress to proscribe certain conduct through explicit prohibitions, and, finally, an accommodation of the law's limits through a clearly delimited but accountable slush fund available to combat financial crises.

Caveats

Before turning to the substance, it is worth briefly noting what this book is not. Most important, this is not a book about why crises happen or how they can be prevented. Those questions are now the objects of impressive amounts of attention, both in and out of academia. Some people are so focused on assigning blame for a failure to prevent the crisis to deregulation, affordable

housing policy, or whatever other cause is their *bête noire* that they may find a failure to address these questions to be a grave offense, but I must simply plead guilty to it. I have chosen to focus my attention on the legal and political dynamics of crisis response.

Nor does the book offer a personality-driven narrative; many excellent firsthand and journalistic accounts have already covered that ground. Chapters 3 and 4 do provide mostly chronological coverage of the events of 2008, but where others understandably emphasize a good story, I emphasize precise legal detail so as to be able to carefully consider legal disputes.

As noted above, this book is also not meant either as a condemnation of or an apologia for the crisis responses. In both cases, this is likely to be a disappointment to some readers. But the book may seem especially misguided to those who bring strong prior beliefs that the bailouts did nothing to help the financial system or broader economy—either because the interventions chosen were badly misguided or because the threat posed by the financial crisis was highly exaggerated. Conventional wisdom has already largely rejected these views, and I accept the general consensus in favor of the revisionist accounts.

Finally, this book omits a discussion of a large and important topic that is central to legal questions surrounding the response to the financial crisis: prosecutors' choices about whether to bring charges, settle cases, and seek criminal convictions for the conduct of financial institutions that contributed to the crisis. This would make an excellent topic for a different book written by someone whose legal expertise about mortgage fraud, fiduciary duties, and consumer protection issues far exceeds my own. Several subjects cry out for an analysis that combines both legal and political elements, including the legal treatment of "robo-signing," the Mortgage Electronic Registration Systems corporation, and the failures to enforce existing regulations leading up to crisis that have led critics to discern a widely followed doctrine of "too big to prosecute." Although I occasionally note the way that negative feelings about these developments affect overall perceptions of government legitimacy, others are more qualified to offer in-depth analyses of these issues.