

Constitutions: Financial Crisis Can Lead to Change

by Thorvaldur Gylfason*

Most constitutions are written or revised following economic or political upheaval of some sort because crises often trigger demands for a fresh start or expose institutional or structural flaws that need to be fixed. After the collapse of communism in 1989-1991, nearly all the countries of East and Central Europe adopted new constitutions. Likewise, following recent turmoil in North Africa, several countries in the region are now preparing to revise their constitutions.

The Norwegian philosopher Jon Elster (1995) describes seven waves of constitution making following the US Declaration of Independence in 1776. First, during 1780-1791, the United States, Poland, and France adopted new constitutions, as did Sweden in 1809 and Norway in 1814. Second, following revolutions in Europe in 1848, several countries adopted new constitutions some of which did not last long, however, because the revolutions producing them were suppressed. Third, after World War I (1914-1918), Poland, Czechoslovakia, and defeated Germany passed new constitutions. Fourth, after World War II (1939-1945), Italy and Japan had new constitutions essentially dictated to them by the allies while Germany, also under allied pressure, adopted a new constitution in 1949. Fifth, as the sun set on the colonial empires of the United Kingdom, France, and others after 1945, new constitutions were adopted in Asia and Africa. Sixth, authoritarian regimes in Southern Europe were driven from power in 1974-1978 and Greece, Portugal, and Spain adopted new democratic constitutions. Seventh, East and Central Europe saw about 25 new constitutions take effect after the collapse of communism 1989-1991, all except Hungary which waited until 2012.

This pattern notwithstanding, financial crises have not in the past given rise to new constitutions. The Great Crash of 1929 was followed by changes in laws that erected firewalls between commercial banking and investment banking. This was the chief aim of the Glass-Steagall Act of 1933 which also set up the Federal Deposit Insurance

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Corporation coupled with the establishment of the Securities and Exchange Commission in 1934. If, instead, the Glass-Steagall Act had taken the form of a constitutional amendment, the dismantling of Glass-Steagall through the Gramm-Leach-Bliley Act of 1999 would have been more difficult. A constitutional amendment might have been more effective. If so, Lehman Brothers might still be around.

Iceland is an exception to the rule that financial crises do not trigger new constitutions or constitutional amendments. Yet, Iceland's financial crash in 2008 had deep roots, so deep that the crash is perhaps better described as systemic rather than merely financial. This is why people took to the streets, banging their pots and pans. The Pots-and-Pans Revolution demanded, among other things, a new, or at least revised, constitution. This does not necessarily mean that a better constitution would have prevented the crash of 2008. However, in view of the several weaknesses of the provisional constitution from 1944, including inadequate checks and balances between the three branches of government, insufficient freedom of information, and the constitutionally protected bias built into the electoral law in violation of the principle of 'one person, one vote,' the crisis made it possible to overcome inherent political resistance to rewriting the constitution with a view to both remedying present flaws and reducing the likelihood of another crash.

This article tells the story of the [constitutional bill](#) that emerged from Iceland's 2008 crash (for a more detailed account, see Gylfason 2012). Following a brief description of the collapse and its background, the article outlines the process and method used to prepare the bill, including the role of crowdsourcing. Next, the article presents some of the substantive highlights of the bill. The article concludes by discussing some of the obstacles that must be overcome for the bill to become the law of the land and by drawing some parallels between Iceland in 2011-2012 and the United States in 1787-1788.

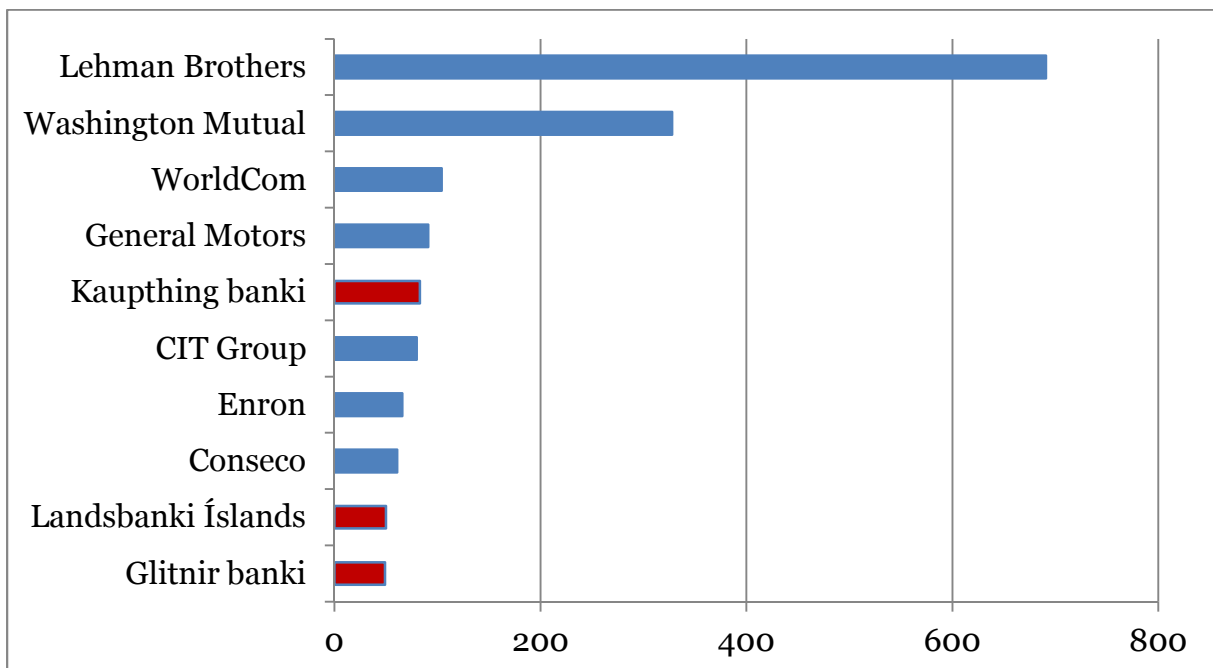
1. Collapse

When countries crash, a natural thing for them to do, among other things, is inspect their legal foundation to look for latent flaws and to fix them. Unsurprisingly, this was one of the demands of the Pots-and-Pans Revolution that shook Iceland after the crash in October 2008. Three banks comprising 85 percent of the banking system collapsed within a week and the rest fell in quick succession. The local equity market was virtually wiped out overnight. Consider civil aviation. Around the world, every air

crash is investigated in the interest of public safety. Representatives of the aviation industry do not ask us to ‘turn the page.’ No, we leave no stone unturned. We need – and insist as a matter of course – on credible crash analysis.

The Iceland crash was a big one, by some measures the biggest financial crash on record. Financial losses inflicted on creditors, shareholders, and depositors abroad and at home equaled about seven times Iceland’s gross domestic product (GDP), a world record. The total cost of the crisis to taxpayers, including the cost of recapitalizing the failed commercial banks plus the bankrupted central bank, amounted to 64 percent of GDP, another world record. The three “big” Icelandic banks’ collapse in 2008 would, had they been American, make the list of the ten largest corporate bankruptcies of all time in the United States, a remarkable result in view of Iceland’s population of 320,000 (Figure 1). The main owner of Landsbanki declared \$750 million personal bankruptcy, including \$500 million in loans from Landsbanki. This is one of the biggest personal bankruptcies on record anywhere. Of this owner, the parliament’s Special Investigation Committee report (2010, vol. 2, p. 3) says: “During a hearing, an owner of one of the banks, who also had been a board member of the bank [Chairman of the Board, in fact], said he believed that the bank “had been very happy to have [him] as a borrower”.”

Figure 1. Ten largest US and Icelandic corporate bankruptcies of all time (\$ bn)



Source: [Financial Supervisory Authority](#) – Iceland.

2. Background

Iceland's key constitutional problem is the absence of effective checks and balances that made it possible for the executive branch to dominate parliament and the courts. Three examples will suffice to illustrate the problem.

- On their own, two cabinet ministers decided to enlist Iceland in the “Coalition of the willing” invading Iraq in 2003 without any consultation with, or even possible recourse for, the parliament.
- In 1998, after the Supreme Court of Iceland ruled that the system of fisheries management is discriminatory and, thereby, unconstitutional, the Court reversed its opinion in 2000 under open pressure from same two ministers.
- In all but five years from 1926 to 2008, the two political parties of the above-mentioned ministers ruled the Ministry of Justice and appointed all judges, even if Iceland has a four-plus-party system.

The supremacy of the executive branch over the legislative and judicial branches made it easier for the government to join hands – some would say jump into bed – with the bankers.

First, the government sold their political cronies state banks at modest prices, with distinctly Russian overtones, having granted valuable common-property fish catch quotas to boat owners in similar fashion free of charge fifteen years before. True to form, the government saw to it that the banks would not be bothered by reserve requirements or inquisitive financial supervision. In gratitude, the banks showered the political parties and individual politicians with money as described by the parliament's Special Investigation Committee report (2010, vol. 2, pp. 200-201, and vol. 8, pp. 164-170). When the banks crashed, one in six members of parliament owed the banks more than 1.3 million dollars each at the pre-crash exchange rate of the króna, their average debt being \$12 million. Bill Moyers, the television journalist, told his viewers on PBS on February 13th 2009 that the US financial industry donated \$180 million to political campaigns in 2008, or 60 cents per person. The roughly comparable Icelandic figure, according to the SIC report, not including the above loans, was \$8 per person in 2006, or 14 times as much as in the United States. It does not take extraordinary powers of inductive reasoning to surmise that the boat owners were similarly grateful for the generosity of the politicians granting them *gratis* catch quotas at taxpayers' expense, a practice that prevails to this day even if the

government began, in 2002, collecting nominal fishing fees – a fraction of their true worth – from boat owners.

Iceland's constitution dates from 1944 when Iceland decided unilaterally to separate from Nazi-occupied Denmark, a separation permitted by the union treaty between the two countries from 1918 when Iceland was granted sovereignty slightly short of full independence. Derived from Denmark's constitution hailing from 1849, with a nationally elected president substituted for hereditary King, the Icelandic constitution adopted in 1944 was intended to be only provisional. Parliament promised to revise it no later than 1946, but has failed to do so to date despite repeated attempts. It took the crash of 2008 for the government to decide to convene a Constitutional Assembly to do the job.

3. Process

There are two main reasons for having the Icelandic constitution written by the people rather than by politicians and their lawyers. The first reason is the parliament's long-standing failure to deliver on its promise to revise the provisional 1944 constitution. Secondly, and more importantly, a constitution is intended, among other things, to limit the powers of parliament and to lay out, for example, the method by which members of parliament are elected. These are tasks that would create a conflict of interest if assumed by parliament itself. Further, the parliament may be tempted to write into the constitution too large a role for itself. To cite James Madison (1788): "You must first enable the government to control the governed; and in the next place oblige it to control itself."

Parliament proceeded in three steps. First, it convened a National Assembly comprising 1,000 persons selected at random from the national registry through stratified sampling designed to secure balanced representation of men and women and of different age groups as well as of different parts of the country. The second step was to appoint a Constitutional Committee to gather information, provide analysis, and propose ideas. The committee had seven members from different walks of life (law as well as literature and science), and produced a 700-page report. Third, in a special election 25 Constitutional Assembly representatives were elected from a roster of 522 candidates by the STV (Single Transferable Vote) method designed to ensure that if your preferred candidate has no chance of being elected or has enough votes already, your vote is transferred to another candidate according to your

instructions, thus minimizing the number of ‘dead’ votes. The elected representatives were a good cross section of Icelandic society – doctors, lawyers, priests, and professors as well as company board members, a farmer, a champion for the rights of handicapped persons, mathematicians, media people, erstwhile members of parliament, a nurse, a philosopher, poets and artists, political scientists, a theatre director, and a labor union leader. Political parties and interest organizations did not field candidates. About a half of the elected representatives had no political affiliation. Voter turnout was 37 percent, low by the standards of parliamentary elections, but typical of national referenda in Iceland.

4. Substance

The people wanted change. The conclusions of the National Assembly that, by law, the Constitutional Assembly representatives were expected to consider were cohesive and clear. The answers given to the media by the elected representatives before the election were equally clear. Overwhelmingly, they favored

- Changing the constitution rather than keeping the provisional constitution from 1944 intact.
- Equal voting rights everywhere in the country in a clear protest against the traditional practice of granting voters outside the Reykjavík area significantly disproportionate representation in parliament.
- Public ownership of natural resources in contradistinction to the present system through which vessel owners have since 1984 been granted valuable common-property catch quotas virtually free of charge, a discriminatory practice that constitutes a violation of human rights and that the United Nations Committee on Human Rights, in a binding opinion that cannot be appealed, instructed the Icelandic government in 2007 to discontinue.
- More frequent national referenda with one person, one vote in reaction to the parliament’s perceived subservience to special interests.
- Strengthening the right of the public to information as an answer to Iceland’s pervasive official culture of secrecy.
- Effective checks on the Minister of Justice’s ability to appoint judges on his or her own in view of the fact that, from 1926 to 2008, two of Iceland’s four main political parties, through their exclusive control of the Ministry of Justice, managed to monopolize the appointment of all judges except for five years.

Public opinion polls reflected similar sentiments. There was a broad and unmistakable consensus in favor of significant changes.

The Constitutional Council had four months to do its work. Some thought this was too short a time, perhaps forgetting that the US constitution was written in four months in 1787. The Council decided quickly to start with a clean slate and rewrite the constitution from scratch rather than revise the provisional one from 1944. Even so, and this is important, a basic feature of the 1944 constitution was retained to preserve the continuity and stability of Iceland's semi-presidential form of parliamentary government – a system of government with a nationally elected president with significant power, primarily the power to refer legislation from parliament to a national referendum (Duverger 1980).

The Council also quickly decided to move the chapter on human rights up front to underline their importance and to locate the articles on natural resources and the environment in that chapter to underline their importance and kinship with human rights. In the end, the Council decided to preface the bill by a preamble declaring that “We, the people of Iceland, wish to create a just society with equal opportunities for everyone.” A literal translation from Icelandic sounds better still: “We, the people of Iceland, wish to create a just society where every one of us has a seat at the same table.” Why say this up front? The reason is that Iceland is not yet such a society as becomes clear when we look at two of the key provisions of the bill, both concerning human rights.

First, the bill stipulates equal voting rights everywhere. Why is this necessary? In Iceland's electoral system, the number of votes needed to elect a member of parliament for the Reykjavík area where two thirds of the population reside has been two, three, and up to four times as large as the number of votes needed in rural electoral districts. Unequal voting rights constitute a violation of human rights as pointed out by European election supervisors visiting Iceland at election time. Over the years, the discriminatory election laws imparted a rural bias to national life and led to a lopsided transition from a rigid, quasi-planned economy toward a more flexible, mixed market economy, resulting in a similarly reluctant and slow depolitization of economic life, including the banks that were privatized as late as in 1998-2003, after the privatization of commercial banks in East and Central Europe. This helps explain why it took the crash of 2008 to convince the government to apply for membership in the European Union in 2009. Negotiations about the terms of

accession are underway. The matter will ultimately be settled in a referendum. For more than a hundred years, representatives of rural areas in parliament have blocked equal voting rights as some of them tried to block the promised one-person-one-vote referendum on the constitutional bill under review. The bill also stipulates that voters may vote for persons as well as parties, even across party lists, besides guaranteeing minimal representation of regions.

Second, the article on natural resources states:

Iceland's natural resources which are not in private ownership are the common and perpetual property of the nation. No one may acquire the natural resources or their attached rights for ownership or permanent use, and they may never be sold or mortgaged. ...

On the basis of law, government authorities may grant permits for the use or utilization of resources or other limited public goods against full consideration and for a reasonable period of time. Such permits shall be granted on a non-discriminatory basis and shall never entail ownership or irrevocable control of the resources.

The bill makes a key distinction between ‘property of the nation’ and ‘property of the state.’ State property – e.g., office buildings – can be sold or pledged at will by the state. Several countries define natural resources as state property – e.g., China, Kuwait, Mozambique, and Russia. The property of the nation is different in that it “may never be sold or mortgaged.” This is because the present generation shares natural resources belonging to the nation with future generations, and, therefore, in the spirit of sustainable development, does not have the right to dispose of the resources for its own benefit. National ownership of cultural assets as well as of (renewable) natural resources, stipulated in the bill side by side, is intended to impose on the current generation an obligation to preserve the assets in question for unborn generations. State ownership involves no such obligation.

The human-rights aspect of natural resources has three main ingredients.

First, the right of the people to their natural resources is a human right proclaimed in primary documents of international law and enshrined in many national constitutions (Wenar 2008). Thus, Article 1 of the International Covenant on Civil and Political Rights states that “All people may, for their own ends, freely dispose of

their natural wealth and resources ...” The first article of the International Covenant on Economic, Social and Cultural Rights is identical.

Second, the Supreme Court of Iceland ruled in 1998 that the Icelandic system of fisheries management is discriminatory and unconstitutional even if, two years later, the Court reversed its opinion under political pressure.

Third, in 2007, the UN Committee on Human Rights expressed agreement with the 1998 verdict in a binding opinion declaring the inequitable nature of the fisheries management system to constitute a violation of human rights and instructing the government of Iceland to rectify the situation as Iceland must do as signatory of the International Covenant on Civil and Political Rights. Even so, the government has not yet responded except perfunctorily to the instructions by the UN Committee.

In addition to the key clauses on ‘one person, one vote’ and public ownership of natural resources, the bill contains several other important provisions concerning transparency and the right to information, environmental protection in a human-rights context, and checks and balances, including the institutional framework surrounding the appointment of judges and other public officials. The bill aims to stamp out corruption and secrecy, yet leaves both words unspoken. At the same time, the bill aims to preserve and strengthen the semi-presidential form of parliamentary government laid out in the provisional constitution from 1944.

5. Send in the crowds

The Council decided to invite the people of Iceland to participate in its proceedings *via* the Internet. This decision was a natural one in view of the fact that the constitutional revision process was set in motion by the Pots and Pans, ordinary people from all walks of life who took to the streets after the crash. There was interest. After all, 522 persons had contested the 25 seats in the Constitutional Assembly. So, conducting Council meetings live on the Internet and inviting the public to peruse and respond to the Council’s written work step by step was a natural thing to do. This was a good way to harness the enthusiasm and expertise of ordinary citizens.

The work was done in three overlapping rounds. Each week, the Council posted on its website some new provisional articles for perusal by the public. Two to three weeks later, after receiving comments and suggestions from the public as well as from experts, the Council posted revised versions of those articles on its website. In a final

round, proposals for changes in the document as a whole were debated and voted upon article by article and the final version of the bill was prepared. At the end of the last round, each article was approved by an overwhelming majority of votes with only a small number of dissenting votes or abstentions. The acceptance of the two key provisions – ‘one person, one vote’ and public ownership of natural resources – was followed by spontaneous applause. The bill as a whole was passed unanimously, by 25 votes against zero, a remarkable result considering the quite far-reaching and radical reforms proposed in the bill.

The invitation extended to the public to contribute to the Council’s work was well received. The Council received 323 formal proposals all of which were discussed and answered by one of the Council’s three committees. More than 3,600 comments were posted on the website by visitors, including some from abroad. Council members answered many if not most of them. Nearly all the proposals and comments received proved useful in one way or another, both what was said and what was left unsaid. If no one objected to the provisional articles posted on the website, then perhaps the Council was on the right track. Almost invariably, the proposals and comments were courteous. Fears that an open Council website might be drowned in gibberish, or worse, proved groundless. Direct webcasts, also aired on TV, were regularly watched by about 150-450 viewers. Over 50 interviews with Council members and others concerned were posted on YouTube. They had, by late 2011, been viewed 5,000 times. Again, bear in mind Iceland’s population of 320,000.

At the same time, many experts advised the Council every step of the way, lawyers and others, in meetings as well as in written memoranda. The Council could not seek the advice of all available and eligible experts. However, like everyone else, those who had points to make were welcome to do so. The Council did not invite representatives of interest organizations to special meetings, but these organizations – bankers, boat owners, farmers, politicians – had the same access as everyone else to the Council, its open meetings, and to individual Council members. This was an important benefit of the crowdsourcing aspect of the operation: it created a framework for inviting everyone to have a seat at the same table, something that special interest organizations in Iceland are not used to. For example, the fisheries legislation ruled unconstitutional by the Supreme Court in 1998 and by the UN Human Rights Committee in 2007 is known to have been originally drafted by the Federation of Icelandic Fishing Vessel Owners. If the vessel owners are unhappy with, for example,

the article on natural resources, they may have to be reminded that they had the same access to the process as everyone else.

With the world's largest per capita number of Internet users, or 95 percent, Iceland could experiment with constitutional crowdsourcing without concerns being raised about unequal access. The unconnected five percent are disproportionately old people, but they could make their views known through ordinary mail and by telephone because the addresses and phone numbers of all 25 Council representatives were made public. Thus, the democratic gains from the experiment seem to easily outweigh potential losses from slightly unequal access. Whether the same can be said of, say, Turkey with 35 percent Internet access, is uncertain. Perhaps the well-connected minority of young people in Turkey and elsewhere in the Near East and North Africa merits a favorable position to sway the new constitutions of the region under preparation in the direction of democracy and human rights.

6. Obstacles

The Iceland bill faces serious political obstacles. According to the 1944 constitution, changes to the constitution need to be approved by two successive parliaments with a parliamentary election in between. Parliament has scheduled a consultative national referendum on the bill in October 2012 at the latest, making it difficult to believe that a new parliament would reject a constitutional bill approved by the people in a referendum. Even so, some members of parliament and others have at least three strong reasons for not wanting to see the bill go through.

First, the article stipulating equal voting rights will probably make some members of parliament unelectable because they are the products of an electoral system allowing political parties to allocate 'safe seats' to candidates with limited following. Asking them to support the bill is a little like inviting the turkey to vote for Thanksgiving. Iceland's political parties tend to behave like interest organizations of politicians.

Second, the article on public ownership of natural resources will not please some members of parliament either because, to quote a former newspaper editor, a keen observer, "it means political suicide to rise against the quota holders in rural areas."

Third, the purpose of any constitution is, *inter alia*, to spell out the rights of the people *vis-à-vis* the state and other citizens. One person's right implies another person's duty.

- The stipulation of ‘one person, one vote’ aims to reduce the political influence of those whose votes have carried extra weight in past parliamentary elections. Rural voters are being asked to give way to others to promote equality.
- The declaration that natural resources belong to the people is intended to redistribute economic power and political clout away from those who in the past were granted free, or, more recently, nearly free, access to fishing quotas, a common property resource by law. Privileged boat owners are being asked to give way to others for the sake of equality and justice.
- The clause on environmental protection aims to hold back those who want to be able to go on polluting the natural environment with impunity. Polluters are being asked to yield. Further, the clause states: “Previous damage shall be repaired to the extent possible.”
- The clause on the right to information aims to restrain the behavior of those who hitherto have benefited from operating under a veil of unhealthy secrecy, enabling politicians, for example, to take out multiple pensions.

Any constitutional referendum involves a contest between narrow special interests and the more widely dispersed public interest, often an unequal contest because special interest groups tend to be more focused, better organized, and better financed. Even so, according to recent opinion polls, 75 percent of electorate want to vote on the bill (October 2011) and 67 percent support the bill (April 2012).

The [bill, available in English](#), has been in public domain for ten months. During this period, no significant, concrete, technical criticisms have been voiced against it, nor have any technical flaws been exposed. Voices critical of the bill seem to echo special interests (boat owners, politicians) keen to preserve the *status quo* for their own benefit, dressing up their political opposition in legal jargon. The national referendum that parliament had resolved to hold concurrently with the presidential election on 30 June was derailed by filibuster in parliament. Following further filibuster that petered out, parliament decided in late May 2012 with 36 votes against 16 with 11 abstentions to hold an advisory referendum on the bill no later than 20 October 2012.

7. Parallels

The similarities between Iceland in 2011-2012 and the United States in 1787-1788 are interesting to note. In the United States, the constitutional bill also took four months

to write and it was put to a series of votes within a year or so of the close of the Constitutional Convention in Philadelphia, following intense political debate and an outpouring of political writing the like of which the country has never seen before or since (Maier 2010). Naturally, the bill created controversy.

Congress decided to refer the bill to the thirteen states for acceptance or rejection. The Constitutional Convention had resolved that acceptance by nine states would suffice for the bill to take force as the country's constitution. Congress agreed. Some thought that Congress had to accept the bill first, but that view was rejected. The Constitutional Convention – with appointed representatives, not elected ones – had drafted the bill and Congress did not consider it appropriate to take a stand on the bill, let alone amend it, for that was for the states to do, not Congress. Some were of the view that by not taking a stand Congress was declaring its consent. Others held the opposite view that by not taking a stand Congress was, in effect, expressing its disapproval.

The thirteen states sent the bill either to their legislatures or to special assemblies for acceptance or rejection. Delaware held the first vote, unanimously accepting the bill in December 1787. A few days later, Pennsylvania passed the bill with 46 votes against 23. New Jersey and Georgia passed the bill unanimously shortly afterward. In January 1788, Connecticut passed the bill 128:40. In Massachusetts, the sixth state to vote, in February, the bill was approved by a narrow majority of 187:168. In April, Maryland said Yes 63:11 as did South Carolina in May 149:73. In June, New Hampshire passed the bill by ten votes, 57:47. With nine states backing the bill, the coast was clear nine months after the Constitutional Convention had delivered the bill to Congress. A few days later, Virginia, the most populous state, approved the bill 89:79. In July, New York said Yes 30:27. North Carolina rejected the bill 184:83, but this made no difference. Rhode Island, the thirteenth state, passed the bill in May 1790 43:32, even if the bill had been overwhelmingly rejected by 2,708 votes against 237 in a general plebiscite. So, if six more people in New Hampshire had voted against the bill, another six more in Virginia, two more in New York, and six more in Rhode Island – twenty people in all – the bill would have been rejected, other things being the same.

The making of the US constitution was no bed of roses, but the bill was passed in a timely manner. The Federalists defeated the anti-federalists, in some states by narrow margins, true; in some, they lost. Some of the views of the anti-federalists

later found their way into the constitution as amendments, however. Democracy prevailed. May democracy also prevail in Iceland.

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