

# Low-Cost Institutions: The New Kids on the Global Governance Block

Written by Kenneth W. Abbott and Benjamin Faude

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Why did states establish the Financial Stability Forum (FSF) in 1999, when numerous inter-governmental institutions, including the International Monetary Fund, World Bank and Organization for Economic Co-operation and Development, were available to promote financial stability? Why did states create the Proliferation Security Initiative (PSI) in 2003 instead of modifying the United Nations Convention on the Law of the Sea, even though doing so left them without authority to interdict high-seas shipments of weapons of mass destruction? Why did states form the Financial Action Task Force (FATF) in 1989 to combat money laundering, despite the availability of capable institutions including the IMF, OECD and regional security organizations? Why did the World Bank, with member state approval, partner with private sector participants in the Prototype Carbon Fund (PCF) in 1999 to support market-based climate change mitigation mechanisms, instead of acting through the Bank itself or the United Nations Framework Convention on Climate Change? In all these cases, states chose to address emerging cooperation problems not by assigning them to incumbent formal intergovernmental organizations or multilateral treaties, but by creating new institutions of different types, including informal intergovernmental organizations (PSI and FATF), a trans-governmental network (FSF), and a transnational public-private partnership (PCF).

These examples point to a larger trend. Over the past three decades, the number of informal intergovernmental organizations (IIGOs) rose from 27 to 72, a 167% increase (see Vabulas and Snidal 2013); transnational public-private partnerships (TPPPs) increased from 26 to 167, a 542% increase (see Westerwinter 2016: 2); and trans-governmental networks (TGNs) expanded from 25 to 141, a 464% increase (see Abbott et al. 2018: 10). At the same time, the adoption of multilateral treaties has stagnated: while some 35 treaties were deposited with the UN in each decade between 1950 and 2000, only 20 were deposited between 2000 and 2010, and none between 2011 and 2013 (Pauwelyn et al. 2014: 734-735).

In a forthcoming paper, we propose to treat IIGOs, TGNs and TPPPs as important members of a common and distinct class of transnational institutions we call “low-cost institutions” (LCIs). In this article, we outline why it is analytically fruitful to treat these seemingly diverse institutional forms as a common class. More precisely, we explain what different forms of LCIs have in common, why governance actors choose to create them, and how their proliferation impacts global governance.

### What Do LCIs Have in Common?

All types of LCIs share two characteristic institutional features. First, they are relatively *informal*, compared to treaty-based institutions. Informality reflects two major traits. LCIs are *created* by non-binding agreements or understandings, not by legally-binding treaties; by implication, they also have authority to *adopt* only non-binding standards, not legally-binding rules. And LCIs feature decision-making formalities and operating procedures that are less elaborate and complicated than those of treaty-based institutions. The second characteristic feature of LCIs is participation by executive, bureaucratic and societal actors, rather than or in addition to states. Together, these features constitute LCIs as a distinct class of international institutions, in spite of the differences among individual forms.

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## Why Do States and Other Governance Actors Choose to Create LCIs?

Decisions to address emerging cooperation problems through LCIs instead of incumbent treaty-based institutions are based on four common rationales, which reflect the common institutional features of LCIs introduced above.

First, the *costs* of creating, operating and changing LCIs, as well as the sovereignty costs they impose and the costs of exit from them, are all, on average, substantially lower than those of treaty-based institutions. All of these low costs derive primarily from LCIs' *informality*: their reliance on non-legally binding obligations and relatively uncomplicated operating procedures. In the G20, for example, "states are unencumbered by procedures and less concerned that their commitment will be strongly binding" (Viola 2015:27). Informality reduces both the international transactions costs and the domestic approval costs of forming new LCIs.

Second, LCIs provide *specific governance benefits* – not equally available through treaty-based institutions – that derive directly from their low costs. These include malleability, flexibility and reduced risk, as well as relaxed constraints on state action. *Participation* by executive, bureaucratic and societal actors (in IIGOs, TGNs and TPPPs respectively) contributes governance competencies and enhances LCIs' ability to target and engage infra- and non-state actors. States and treaty-based institutions often design and sponsor LCIs, such as the PCF and the International Partnership for Energy Efficiency Cooperation, to reap these benefits, helping them to address specific governance problems (substantive fit) at acceptable costs and risks (political fit).

Third, LCIs offer many of the *general governance benefits* provided by treaty-based institutions, although sometimes in attenuated form. For example, LCIs can reduce the transaction costs of cooperation, mitigate asymmetric information, enable working relationships among officials, establish relatively stable behavioral expectations, and construct actor reputations (see Keohane 1984). For example, states created the FSF to facilitate interactions among senior financial policymakers that were more forthright and wide-ranging than could be achieved in formal intergovernmental organizations (Clarke 2014).

Fourth, LCIs *empower* their infra-state and non-state *participants* by enabling them to play direct roles in global governance: IIGOs empower executive officials (e.g., vis-à-vis legislatures), TGNs bureaucratic actors, and TPPPs societal actors. Participating in a TGN such as the International Organization of Securities Commissions (IOSCO), for example, "helps independent regulators minimize [domestic] political interference in their affairs while building up their reputation and authority" (Farrell and Newman 2016:716, 722-723). Empowerment incentivizes those actors to favor the creation of LCIs (of the appropriate type) when they pursue transnational cooperation.

Taken together, these four factors – low costs, specific and general governance benefits, and empowerment – explain why states create LCIs to address cooperation problems rather than assigning those problems to incumbent treaty-based institutions, and thus why LCIs have proliferated. States also create LCIs such as the FSF, FATF and PCF to complement incumbent treaty-based institutions rather than to replace them. For example, states concerned with weapons proliferation created the Australia Group to complement the legally-binding chemical and biological weapons regimes by facilitating technical interactions among national experts (Vabulas and Snidal 2013). This institutional "layering" allows states to create mutually reinforcing divisions of labor (Gehring and Faude 2014).

However, the same institutional features responsible for LCIs' low costs and specific governance benefits constrain LCIs' ability to address demanding cooperation problems. LCIs are less highly institutionalized than treaty-based institutions, and so cannot offer the same centralization of cooperative activities and institutional independence (Abbott and Snidal 1998). More specifically, LCIs cannot adopt legally-binding rules or implement strong monitoring and enforcement. As a result, they cannot tackle issues that require highly credible commitments to overcome incentives to defect, as in international trade. Thus, LCIs are sub-optimal institutional choices in settings where distributional conflicts are strong, defection from cooperative solutions is likely, and noncompliance is difficult to detect. Under these circumstances, treaty-based institutions are the best institutional choice.

Nonetheless, the current gridlock in many treaty-based institutions (Hale et al. 2013), and the current polarization in inter-state relations, make treaty-based institutions less available to address emerging cooperation problems. These

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conditions likewise make changing incumbent institutions to fit emerging cooperation problems more difficult. Significant change usually requires unanimous decisions, which are difficult to achieve given multiple veto players and high transaction costs, especially in periods of polarization. These conditions make cooperation through LCIs more attractive even where it is second-best.

And LCIs may in fact be especially conducive to facilitating cooperation when political opportunity structures are malign (Underdal 2002), characterized by a breakdown of trust and reliance on specific reciprocity (Keohane 1986). Under these conditions, LCIs offer two distinct pathways to modest cooperation. First, even where relations among national leaders are polarized, those leaders may accept the need for continued international cooperation in limited areas, e.g., technical cooperation on cross-border interactions. LCIs are well-suited to advance such cooperation, and to do so with limited publicity, minimizing leaders' audience costs with supporters. Second, where polarization and distrust are concentrated at the level of national leaders, lower-level officials, as well as non-state actors, may retain more cooperative preferences; they can advance these preferences through LCIs to the extent they have sufficient political space for independent action.

Both pathways depend on the fact that cooperation through LCIs often flies "under the radar:" the general public is simply unaware of many IIGOs, TGNs and TPPP, as they are formed without high-level executive clearance or legislative approval, and their activities are technical in nature. While reduced visibility raises legitimacy concerns, in malign political opportunity structures it holds out hope for modest levels of socially beneficial cooperation. To be sure, the second mechanism presupposes that leaders do not prevent lower-level officials from participating in LCIs. Yet LCIs are not invisible; capable leaders committed to stamping out cooperation can identify and block their actions. Thus, this mechanism is more likely to operate where leaders' antagonism reflects political strategies rather than sincere beliefs, and where leaders lack the resources or competence to police all forms of governance.

LCIs are also used by sub-groups of states that seek outcomes others may oppose. For example, states that support a particular level of cooperation can create a new LCI to (at least partially) bypass defenders of the status quo – or those lacking the political will for enhanced cooperation – in an incumbent treaty-based institution, a common strategy for actors facing "legislative gridlock" (Thelen 2003: 226). LCIs are well-suited to this strategy because they lack strong norms of multilateralism, allowing states to exclude "spoilers" while including like-minded actors (Eilstrup-Sangiovanni 2009).

LCIs are thus often used to organize "coalitions of the willing" within larger groups of states, as the PSI and Australia Group were. Similarly, states may use an LCI to bypass *opponents* of the status quo, who might otherwise force unwelcome change in an incumbent institution. The US did so in relinquishing control over the Internet Corporation for Assignment of Names and Numbers (ICANN), making it an independent private body (Becker 2019).

Similarly, rising powers may exert influence through LCIs so as not to pose direct challenges to incumbent treaty-based institutions, and thus to their member states. During the coronavirus pandemic, for example, China has provided medical equipment and supplies to numerous countries, including Spain and Italy, through its Health Silk Road initiative, a loosely-structured web of bilateral relationships. These actions help China advance its preferred model of global health governance, without directly challenging the World Health Organization.

## How Does the Proliferation of LCIs Impact Global Governance?

The availability of LCIs reduces the institutional status quo bias of global governance. Our analysis suggests that the composition of global governance institutions will continue to change over time to include an expanding proportion of IIGOs, TGNs, TPPP and other low-cost institutional forms. LCIs are highly malleable, providing states and other actors an expanded palette of governance options. They are also highly flexible, so that they can be modified at low cost as circumstances change. LCIs thus allow states to fine-tune governance arrangements to the substantive and political characteristics of particular problems, and to modify them as problems or demands for governance evolve, or as current arrangements prove unsatisfactory. For example, in 2009 the G20 states were able to quickly restructure the FSF, now known as the Financial Stability Board (FSB), to respond to the 2008 financial crisis. Over time, the emergence and differentiation of LCIs should facilitate more nuanced global governance (Zürn and Faude

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2013).

LCIs offer pathways for states to at least partially overcome the dysfunctional procedures and gridlock that currently characterize many treaty-based institutions (Hale et al. 2013). They allow states to bypass burdensome decision procedures, avoid veto players, and increase support for cooperation by fine-tuning governance arrangements to problem characteristics, contextual features and political sensitivities. For example, the G20 was created to manage global financial reforms without the “layers of rules and procedures” in the IMF that made “quick, flexible and innovative policies difficult to achieve” (Viola 2015:27); and the European Competition Network was intended to bypass the “administrative bottlenecks” created by centralized European Commission decisions on cartel cases (Danielsen and Yesilkagit 2014). LCIs also facilitate compromise among states with different circumstances, preferences and power. Where political opportunity structures are malign – as in the current period of polarization and tension – LCIs provide opportunities for modest forms of cooperation.

Contemporary global governance is highly institutionalized, so most LCIs are intended to complement incumbent treaty-based institutions. Such layering further broadens the palette of governance options, and often produces the best outcomes, especially for multi-faceted problems, as each institutional form can address those aspects of the problem for which it is best-suited. LCIs, for example, can focus on activities such as coordination, information, trust-building, non-state actors and experimentation, while leaving to treaty-based institutions the creation of credible commitments and enforcement.

At the same time, LCIs are in some sense competitors to treaty-based institutions. While direct competition is rarely intense, LCIs do provide alternatives to incumbent treaty-based institutions for states choosing governance arrangements. Where states prefer LCIs, their choices reduce the focality of incumbent institutions, individually and as a class, potentially weakening the scope of their authority. Such choices also increase governance complexity, which may have negative as well as positive consequences. Finally, states may choose LCIs for political reasons – e.g., to reduce constraints or to signal action without taking costly steps – where incumbent treaty-based institutions would govern more effectively. In the aggregate, however, the proliferation of LCIs produces a more diverse and variegated global governance system.

Finally, LCIs empower their executive, bureaucratic and societal participants. This empowerment is changing the patterns of authority in global governance and its actor composition, in parallel to ongoing changes in institutional composition. Given their rapid proliferation, LCIs appear to have been more responsible for these changes in authority than state delegation to non-state actors, and as responsible as entrepreneurial activities by non-state actors (Green 2014). Because empowerment incentivizes infra- and non-state actors to promote LCIs, we expect governance authority to continue to diversify.

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