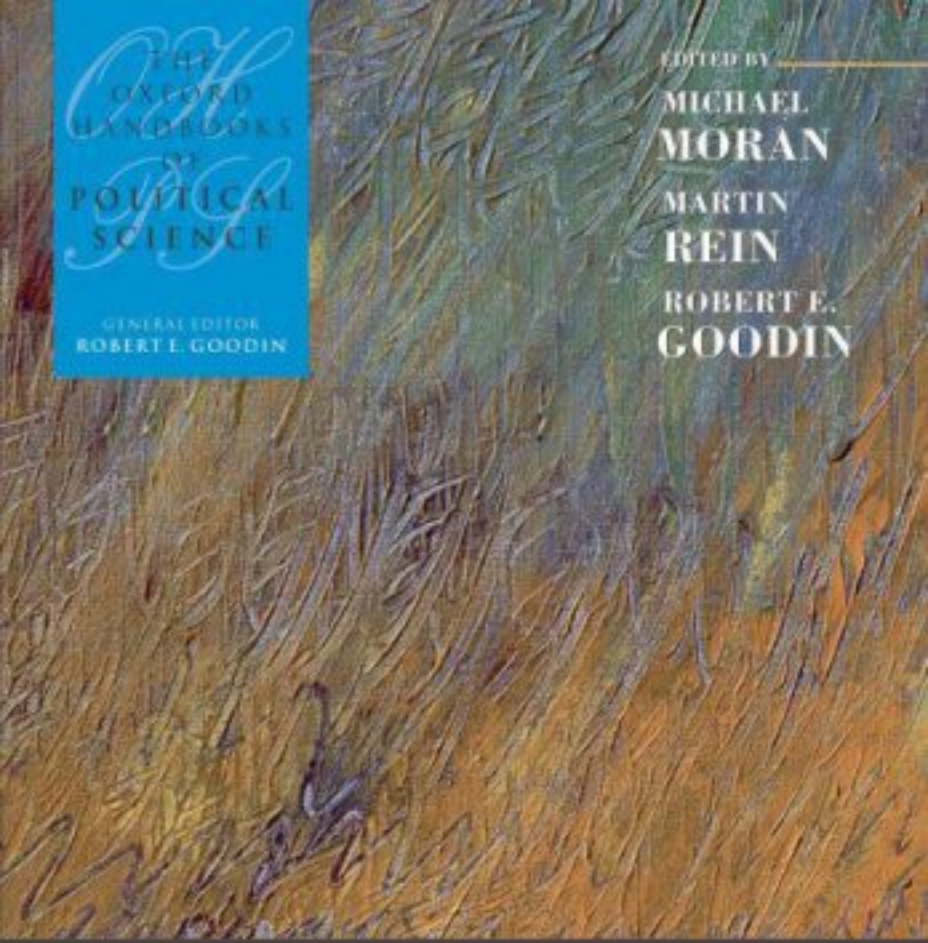

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maintain the public ardor that created the pressure for the income–leisure swap in the first place, its impact may be severely degraded over time, while imposing administrative costs that could, in the aggregate, make the policy worse in practice than no policy at all.

This analysis touches the very core of political theory. The inheritors of Rawlsian political philosophy rarely consider the shape and character of the political institutions that will be created to bring into practice the distributive preferences deduced from behind the veil of ignorance. But those reasoning about justice in ways intended to connect to the real world need knowledge of the predictable effects of the operation of actual political institutions. (An important exception to the absence of sophisticated analyses connecting political theory and institutional design is Rothstein 1998.)The shape of desirable redistribution may be altered by a recognition not only of what actual political institutions will do with the demand for extensive redistribution, but also what institutions so empowered will be able to do to (and perhaps for) citizens when their scope has been increased. Ultimately, normative political economy must grapple with institutional and political questions.

Public policy, institutional analysis, and political philosophy do not deal with three distinct subject matters; rather, they are three different attempts to deal with the problem of how human beings ought to govern themselves. The world will not be well governed until the statesmen learn to pay attention to the results of careful thought and the thinkers take the problems of statesmanship seriously.

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CHAPTER 32

PRIVATIZATION AND REGULATORY REGIMES

COLIN SCOTT

1. Introduction

Regulation, both as public policy instrument and as field of investigation, was apparently an area of dramatic growth in the last quarter of the twentieth century. The policy boom may be explained in part by a loss of confidence in traditional mechanisms of public ownership in many fields of public service delivery in OECD countries. This disenchantment was combined with a perception that public ownership was a drag on fiscally constrained economies, whereas selling off assets provided positive fiscal benefits. Policies of privatization (defined narrowly in this chapter as transfer of ownership of state assets—see the analytical discussion of wider conceptions of privatization by Feigenbaum, Henig, and Hamnett 1999, 8–11) were accompanied by processes of public management reform within bureaucracies. These reform processes have, in many countries, liberalized some aspects of central public management, while at the same time being accompanied by the creation of new layers of regulation over public sector activities, frequently in new or remodeled free-standing agencies (Hood et al. 2004).

The focus on regulation as the problem of control for sectors where ownership was transferred from public to private sector stimulated the identification of other, long-established policy processes (for example in financial services and health care sectors and over economy-wide issues such as occupational health and safety, consumer protection, and the environment) as also belonging to the set of regulatory activities. Consequently there has been much for scholars in the relatively new field of regulation to examine, even though many of the phenomena were not exactly new.

* I am grateful to Martin Lodge for comments on an earlier version of this chapter.

The central concerns of the public policy literature in understanding this transformation in governance have been with the emergence of the regulatory state (Braithwaite 2000; Majone 1994*b*; Moran 2002, 2003; Sunstein 1990), and with the qualities and problems associated with regulatory agencies (Macey 1992; Thatcher 2002; Thatcher and Sweet 2002). This focus within the political science literature may partly be explained by the interest within the discipline in formal state institutions, which generates a concern to map an apparent shift in power from government departments to autonomous agencies, linked to privatization policies which have swept through the OECD since the early 1980s.

The risk faced by the discipline in focusing on these two linked dimensions of regulation, the regulatory state and agencies, is that this model of regulation as an instrument of governance may obscure as much as it illuminates. More specifically the approach is open to the criticism that it assumes too strongly the transfer and adoption of public policy institutions and processes which it may be argued, are peculiar to the United States and unlikely to be replicated elsewhere. It is ironic that the policy boom in regulation occurred at a time when the agenda in the USA was geared towards attempting to dismantle a good part of its regulatory heritage through programmes of deregulation. Even before regulation as an instrument of government had matured elsewhere, the OECD was calling for extensive regulatory reform (OECD 1997*b*).

One way to reconceptualize the field, developed in this chapter, is to conceive of the institutions, norms, and processes of regulation in a somewhat broader way than is suggested by the American model of public regulation of business by agencies. According to this reconceptualization regulation occurs within "regimes" characterized by diffuse populations of actors and considerable diversity in the norms and mechanisms of control. The concept of regimes facilitates us in making a link between regulation, with its traditional narrow conception of state institutions and laws, and contemporary analysis of governance. A governance narrative emphasizes the fragmentation of regulatory power in contemporary policy processes. This approach is skeptical about the possibility of wholesale delegation of regulatory power to agencies and is more open to the possibility that power may be shared and diffused. As regards state organizations and power, this critique notes that outside the United States delegation to agencies commonly involves the substantial retention of power by ministerial departments (Hall, Scott, and Hood 2000). Second it notes an OECD-wide trend towards exerting a substantial degree of oversight over agencies, not just through the courts, but also through central agencies concerned with the promotion of regulatory efficiency.

The "intra-state diffusion of regulatory power" (Daintith 1997) is accompanied and magnified by further diffusion of key regulatory capacities both to supranational governance organizations (Braithwaite and Drahos 2000) and to a variety of non-state actors (Grabosky 1994). This organizational diffusion is coupled with diversity in mechanisms of control to embrace not only conventional hierarchical methods and official non-legal alternatives (such as soft law), but also modalities rooted in the capacities of both community and competitive processes to exert control. Viewed from this perspective the focus on public regulatory agencies exerting control

through legal authority appears incomplete at best, and perhaps seriously misleading for those seeking to understand ideas about regulatory regimes.

2. Regulatory Regimes and Interdependence

There is no consensus in policy or academic circles as to what exactly is connoted by the term regulation. Selznick's classic definition—"sustained and focused control exercised by a public agency over activities that are socially valued" (Selznick 1985, 363–7)—is often cited with approval (Majone 1994*b*; Ogus 1994). But the exclusive focus on public agencies, common within American studies of regulation, is problematic when so much regulatory activity is "decentred" (Black 2001*a*). Many regulatory regimes do not focus on a public agency (whether a government department or independent agency) as regulator, and even where they do such agencies may not have a monopoly over regulatory power (Francis 1993, 43–8).

A strength of Selznick's definition is that it comprehends not only oversight by reference to rules (consistent with the *OED* definition of regulation) but also other forms of control. Empirical analyses of regulatory activities within particular domains do, in many cases, point to a diffusion of regulatory capacities among a range of state, non-state, and supranational actors. Resources relevant to the exercise of power within regulatory regimes include legal authority, wealth, organizational capacity, information, and the capacity to bestow legitimacy (cf. Daintith 1997; Hood 1984).

It has often been observed in empirical studies that regulators rarely use their formal powers of enforcement, and are more likely to use strategies based on education, advice, and persuasion to secure some form of compliance (Grabosky and Braithwaite 1986). Such observations have been used to ground a prescriptive theory which suggests that regulators should generally seek to rely on such low-level strategies, at the base of a pyramid of regulatory enforcement, and only escalate to more formal and coercive measures where lower-level strategies have failed (Ayres and Braithwaite 1992). Even in the case of legal authority, power is liable to be fragmented—a factor which creates problems for the rational and instrumental deployment of regulatory pyramids by agencies (Scott 2004). For example, a regulatory agency may have powers to monitor sectors of the market, to collect information, and to initiate enforcement actions. But it is not unusual to find that legislatures or government departments reserve to themselves powers to make or change regulatory rules, in addition to the wider power to change the regime as a whole. Furthermore it is quite common to find that formal sanctions can only be applied with the consent or decision of a tribunal or a court. Within most systems regulatees may wield formal legal power, for example to consent to rule changes, to make enforceable

undertakings, or through standing to challenge regulatory decisions by means of litigation. Indeed, the formalization of norms within regulatory regimes, a hallmark characteristic of the transition to the regulatory state (Loughlin and Scott 1997), carries with it the risk of juridification and the displacement of effective social norms by a dependence on legal rules which are incapable of grounding such effective control (Teubner 1998/1987). This kind of challenge in the use of law for regulatory purposes has led both to critiques of inherent "fuzzy legality" (Cohn 2001) and prescriptions for "regulation of self-regulation" (Teubner 1984) and proceduralization as mechanisms for escaping from the adverse effects of legalization (Black 2000, 2001*b*).

In many regimes formal legal authority is shared between national and supranational governmental organizations, particularly in respect of standard setting. States are key players within "webs of influence" through which supranational regulatory regimes emerge and develop (Braithwaite and Drahos 2000). But that significance does not lie in the capacity of any individual state to determine the direction taken by a regime; rather there is a range of strategies by which governments may respond to forces over which they exert little control.

In some regimes the legal authority component is constituted not by legislation but by contracts, giving regulatory relations more of the flavour of agreements than hierarchical instruments. Some of these instances of "contractual regulation" are individuated in character—taking the form of agreements between two parties, one of whom, for example a major public or private purchaser, is likely to exert greater power in setting the contractual rules of the game (Scott 2002). In other cases the contractual basis is collective. Thus, while some self-regulation (for example as it applies to legal and medical professions) may be authorized by statute, many self-regulatory regimes are underpinned by contracts between the members of a trade association which empower the association to make and enforce rules against their members. An apparent paradox, never fully taken on board by self-regulation skeptics, is that self-regulatory associations typically wield the full array of regulatory powers—rule making, monitoring, and enforcement—within a single organization, untroubled by the kind of regulatory fragmentation more common in public regulatory regimes. Not all self-regulation is characterized by such monopolistic power, and for Ogus (1995) the potential for competition between self-regulatory organizations offers a means of control over their activities. Such competition is liable to be magnified at the international level where national or regional self-regulatory associations find themselves competing both for credibility and for members with other similar bodies.

The other resources relevant to the exercise of power within regulatory regimes are typically more widely distributed than legal authority. It has long been observed by economists that firms are liable to possess more information than consumers and also regulators (defined as "information asymmetry" (Arrow 1963)), pointing up a particular form of weakness in the capacity of agencies to regulate. In sectors characterized by small numbers of large firms regulatees are also likely to have greater wealth and organizational capacity than agencies, giving them greater capacity to participate effectively in regulatory proceedings or to interpret regulatory rules.

It is not straightforward to offer an a priori suggestion as to which actors are likely to have the capacity to bestow legitimacy on a regime. Under different conditions it may be any of government, agencies, regulatees, supranational organization, or NGOs.

Taken together, the observations that resources relevant to the exercise of power within regulatory regimes are typically widely dispersed, and that much regulatory control is not effected through the application of formal legal authority, suggest the "regulatory regime" may be a more appropriate unit of analysis than the regulatory agency. Regime is a concept borrowed from the study of international relations (Krasner 1983) which highlights the "historically specific configuration of policies and institutions which structures the relationship between social interests, the state, and economic actors in multiple sectors of the economy" (Eisner 2000, 1).

Eisner's regimes analysis, rooted in the context of US regulatory policy in the twentieth century, does focus on the regulatory agency as the basic unit of analysis (Eisner 2000, 15). But he shows that the "market regimes" established during the Progressive era (for example for regulation of competition and interstate commerce) have been followed by further waves of regulation, promoting the role of interest groups in "associational regimes" in the New Deal era and "societal regimes" in the postwar period. Eisner characterizes the emergence of controls over regulation and the deregulation movement which developed from the 1970s as an "efficiency regime" (Eisner 2000, 8–9).

The dynamics within the US polity generating these different structures and rationales for regulation have been interpreted as a product of complex interactions between changing environment, interests, ideas, and institutional histories (Hood 1994). The economic theory of regulation (ETR) developed in the work of George Stigler (Stigler 1971) and Samuel Peltzman (Peltzman 1976) in the 1970s, has been highly influential in the development of a somewhat jaundiced explanation for the development of regulatory regimes by reference to the pursuit of interests. The ETR conceives of regulation as a service provided by government for which there is supply and demand akin to a market. Behaviour for firms, bureaucrats, politicians, and others is explained by reference to the standard economic assumption that individuals are in the rational pursuit of their own utility. These actors all seek "rents" as the rewards for their actions. Though hardly tested empirically (or arguably, capable of being tested) the hypothesis that regulation was likely to be supplied by government to favor those interests willing to pay the most (by means of contributions to election funds, and perhaps also bribes) and would thus nearly always favor large firms rather than serve any conception of the public interest has been influential.

It was something of a problem for the economic theory that it struggled to explain the emergence of social regulation in the postwar period which appeared to favor less wealthy and more diffuse interests such as employees and consumers. The interests-based theory was considerably sharpened by political scientist James Q. Wilson in his coalitional theory. Wilson (1980) suggests that political preferences are more complex than simply the aggregate of society's utility functions, and liable to be shaped through political processes which may yield coalitions on particular issues. Thus, it

is more than narrowly concentrated interests which shape the initiation and development of regulatory regimes.

Proponents of ETR faced another challenge when, rather against the expectations of their hypotheses, the US federal government began dismantling regulation in such industries as trucking, airlines, and telecommunications in the 1970s. One possible response is to suggest that the political system somehow managed to produce a set of outcomes which heroically challenge the apparent inevitability that public policies will be provided to support wealthy interests. A second possibility, perhaps linked to the first, is that ideas of the kind being developed by proponents of ETR and others had themselves become factors shaping the behaviour of actors in developing deregulatory policies (Derthick and Quirk 1985). Peltzman (1989), however, attempted a bold application of ETR to explain the apparent paradox of deregulation. He suggested that the industries which had been subject to deregulation had each experienced reductions in the rents available to the service providers. Consequently major industry players had less to offer politicians and bureaucrats to reward this behaviour and consequently, at some point, the bias of the regime towards favoring industry incumbents tipped to favour others. Put briefly, "[t]he rents supporting the political equilibrium eroded" (Peltzman 1989). He recognizes that this revised account does not appear to provide a universal explanation for what happened. In telecommunications, in particular, he suggests that regulators could have protected monopoly rents for a longer period than they did, and that deregulation is better explained by reference to changing ideas about the performance of the public function by regulatory officials (Peltzman 1989). The strength of the ETR appears to lie in the influence it has had in causing widespread questioning, in both policy and academic circles, of assumptions that regulation serves the public interest. The case for its capacity to explain dynamic processes of regulatory change is, at best, unproven.

European scholarship on the dynamics of regulatory regimes cannot ignore the powerful influence of the literature which has emerged from the context of American regulatory policies and procedures. Some, such as Giandomenico Majone, embrace the American model and doctrines, advocating, for example, substantial adoption of the US model of independent regulatory agencies and suggesting that a process of convergence is already occurring (Majone and Everson 2001). Others are more skeptical. Leigh Hancher and Michael Moran (Hancher and Moran 1989) challenge assumptions about the risk of regulatory capture, showing that within European political systems the diffusion of power within "regulatory space" reduces the applicability of ideas about either *ex ante* capture of the ETR variety or *ex post* capture of the type posited in Bernstein's life-cycle theory of regulation (Bernstein 1951). The concept of regulatory space provides a powerful metaphor for encouraging closer attention to the attributes, ideas, interests, and capacities of the variety of actors found within regulatory regimes (Hancher and Moran 1989; Lange 2003; Scott 2001; Shearing 1993).

The approach also encourages us to think beyond state organizations as regulators. Thus we can incorporate in models of regulation both professional and industry self-regulation, regulation by contract (by both state and non-state bodies), and the work of private standard-setting organizations such as the national standards organ-

izations established in Germany (DIN), France (AFNOR), the UK (BSI), and the United States (ANSI) in the first quarter of the twentieth century, together with their more recent supranational counterpart, the International Standard Organization (ISO, established in 1946). The tendency to treat international regulatory bodies, whether governmental or non-governmental, as somehow "external" can also be countered by linking the regimes approach to ideas of regulatory space.

3. Modalities of Control

It is a weakness within the political science literature on regulation generally that it has paid closer attention to the emergence of regulatory regimes and the policy-making processes surrounding them, at the expense of investigating day-to-day processes of implementation which have largely been the preserve of sociolegal scholarship. In support of closer investigation of how regulatory regimes are implemented, the idea of regulatory space can be given greater analytical clarity by introducing conceptions of control which have been read across from cybernetics. This approach suggests that any viable regulatory regime should have each of the three identifiable components of a system of control (Hood, Rothstein, and Baldwin 2001). Within this analysis any control system must have some rule, goal, standard, or norm (director in cybernetics speak), a mechanism for monitoring or feeding back information about compliance with the rule, goal, standard, or norm (detector), and a means by which deviational performance is realigned (effector). In a classical regulatory analysis these components map onto rules, monitoring, and enforcement. This approach has two particular strengths. First it promotes an analysis which precisely identifies the dispersal of the three components of a regulatory regime around the various actors within the regulatory space. Secondly it encourages us to recognize modalities of control which either supplement hierarchical control (in hybrid forms) or wholly substitute for it. Thus community-based control operates through the emergence of norms in social settings with monitoring through mutual observation of actors within a community and realignment of deviant conduct through the application of social sanctions such as disapproval and ostracization. Within competition-based control, standards emerge through the rivalry of actors jockeying for position in markets or in other settings, information about compliance with the standards is fed back into the system through the implicit monitoring of performance, for example by buyers in markets, and deviant behaviour is realigned by the aggregated decisions of diffuse actors who use information about performance (for example buyers choosing to buy elsewhere, or parents choosing to send their children to different schools).

While the first three modalities of control, hierarchy, competitition, and community, are well established in the literature, albeit with a variety of labels, there is no consensus on the existence of a fourth modality, labelled "contrived randomness" in