The new regulatory state: already a thing of the past?

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Abstract

Should the new regulatory state be reconsidered in the light of the credit crunch? According to the author the concept of the new regulatory state is still a viable one, but in need of correcting. In vital sectors, not too much substantive law should be allowed to leak away from the formal legal domain (and its command and control model) into alternative constructions set up by the local actors involved. And the law itself should provide clear procedures and protect the distinction between public functions and private interests in order to create clarity as to the division of responsibilities. There are three strands to the author's argument. First of all, he gives an account of the development of his personal views on the relationship between the private and the public legal spheres. Secondly, he explains that this development runs parallel to the transformation of the old into a new regulatory state. Lastly, he looks into the critique of the new regulatory state and argues in hindsight of the credit crunch, that some of this critique should be taken seriously.

Key words: regulatory state, law, governance, public interests, credit crisis

1. Introduction

Two years ago in 2006 Gráinne de Búrca and Joanna Scott, the lady champions on law and governance (on both sides of the Atlantic) edited a book called "law and *new* governance in the EU and the US."[1] The book contains a number of case studies drawn from both continents, dealing with forms of alternative governance in a range of areas such as social policy, health care, environmental policy and the combating of discrimination. We read about new forms of standard setting: soft law, rolling rules regimes, benchmarks and positive feedback loops. We learn that these new approaches are not necessarily at odds with the traditional formal law. The relationship between law

[1] My Italics. *Law and new governance in the EU and the US,* Gráinne de Búrca and Joanna Scott (eds.), Hart Publishing, Oregon, 2006.

and new governance can be viewed in a more optimistic and constructive manner. A relationship of fruitful interaction. Perhaps these new forms of governance can even obtain constitutional recognition?

The book I am talking about has been reviewed in the Texas Law Review by a professor at Georgia School of Law, called Jason Solomon.[2] The reviewer is clearly sensitive to the promise of a new regulatory state contained in many of the contributions. He argues that ever since Bill Clinton famously declared the era of big government to be over, the question has been what should come in its place. According to the author we have moved into a mode of collaborative governance where public agencies and private industry representatives work together to define and revise standards. The public/private governance mix as the new solution for the regulatory state of the 21-ste century.

Under any normal circumstance I would have welcomed both the book and the review in the Texas Law Review. As I will explain shortly somewhere in the mid nineties I gave up my resistance against the merging of the private and the public spheres in the law as much as the merging of the law itself with other instruments of public policy. Ever since I have been happy with a new outlook on life that ensued from it. Also I like to think of myself as an optimistic person. Rather than commanding, controlling and punishing, what is there against working together with the private sector in a meaningful and constructive manner? Why stick to the old formal legal approach and not allow ourselves to experiment with new forms of governance?

But then in 2008 came the credit crunch. In the banking sector the new regulatory state obviously failed to perform. Short term gains took preference over long term interests. Too many risks were taken; self regulation obviously did not lead to sufficient self restraint. Old Alan Greenspan last week admitted to it all when he was paraded before the US Congress as in a Stalinist show process: he had been too optimistic about the capacity

[2] Jason. M. Solomon, 'Law and governance in the 21ste Century Regulatory State', *Texas Law Review*, 2008, 820-856.

of self regulation in the financial sector; there was just too much *laisser faire* and *laisser passer*.

In the meantime, Governments have stepped in, buying out bad loans, bailing out banks, at the cost of billions and billions of dollars, pounds and euros. This recipe of robust state interference is not likely to be dished up in the banking sector alone. The banking crisis has become a financial crisis which in its turn has started to affect the real economy. And the more the crisis effects our personal lives and social relationships, the more wide spread will be the calls for state interference. Politicians will react. Sarkozy already announced the end of 'autoregulation'. Gordon Brown speaks of large scale nationalizations. Barrosso proposes that our states should take a golden share in our industry. These men talk like old fashioned socialists! The era of minimal government is over; big government is there once again. It looks as if the new regulatory state of the 21-ste century lasted no longer than 8 years.

Is the new regulatory state really already a thing of the past? This is the theme of my short lecture to conclude our conference. I will argue that it is not but in need of correction. In my view the role of the law and the distinction between public responsibilities and private freedoms within the law should be revaluated. There are three strands to my argument. First of all, I will tell you a little bit about the development of my personals view of dealing with the relationship the public and the private legal sphere. Secondly, I will explain how these views very much run parallel to the transformation of the old regulatory state into a new, as least as it is often perceived by others. Lastly, I will look into the critique of the new regulatory state and argue in hindsight of the credit crunch, that some of this critique should be taken seriously.

2. Some personal observations

I studied law at the University of Amsterdam from 1979 to 1984. This was in the aftermath of the progressive wave set in motion by the student revolts of the sixties. Margret Thatcher and Ronal Reagan had already proclaimed their neo liberal agenda in

the UK and US. But at our law school this past mostly unnoticed. Only after I graduated did the first yuppies, forerunners of the present day fat cats, enter the Amsterdam scene.

However critical the Amsterdam law school was then supposed to be, during my studies I unconsciously developed two deep rooted convictions. The first was that law is good and just and must therefore govern all human activities. The second was that within our legal system there is a divide between private and the public law. This divide is not just the result of an accidental streak of history. It reflects the fundamental characteristics of our societies. Public authorities must simply respond to different rules than private individuals.

As law students we all knew that at some point in our studies we had to make choice either to become a private lawyer or a public lawyer. Very often this choice was not very hard. It is like our love for cats and dogs. You are either a cat person or a dog person. Only very few show a fondness for both of them. And as we know, even then the animals are never really at peace with each other.

In my case, for a long time this inner conviction remained unchallenged. Things only started to change in the nineties, when the old order of communism had been thrown over in order to give way to a new liberal world order. States were there to ensure the proper functioning of the markets and good results would ensue from it.

Progressives and social democrat leaders followed suit, trying to reconcile their traditional preference for a strong state with market values. It was the time of the third way, advocated by politicians like Bill Clinton, in this country Wim Kok and of course the inventor of the very term: Tony Blair. In their time, many public services and enterprises were privatized. But the third way dictated that privatization should not be fully fletched. The states reserved important regulatory powers and were prepared to step in when the public interest so required. Thus in many countries the health care systems, the railways and the post services developed a distinct hybrid taste: neither public, nor private but something in between. And simultaneously, private enterprise was to except

more public responsibilities, not only being accountable to itself and its share holders but to a wider circle of stakeholders in the general public as well.

In this climate I started to realize that my classical view of the distinction of the law was perhaps becoming increasingly obsolete. In 2003, in a publication for the Dutch bi-annual conference on constitutional law dealing with the 'public task' I decided to make a volte face.[3] No longer would I stick to my old dogma's relating to the separation of the private and the public sphere. Instead I would welcome the merging of these spheres as an expression of the new post modern order. Messy but effective.

I must say that I never regretted my new stance. It opened windows and gave new inspiration. Instead of constantly nagging along the sideline that the legislature and politicians are messing things up, it allowed me to adopt a more constructive attitude in commenting upon legal changes. The state should be allowed to experiment with new forms of government, whether private or public, inside or outside the law. In the end what matters is whether these forms of governance work out in practice and contribute to the realization of the public interest and fundamental rights. Whether it does depends on the outcomes of objective research, thus, the new regulatory state not only has a practical, but also a rational touch. Social scientists and legal researchers are engaged in its evaluation and must come up with new recommendations.

3. The new regulatory state

"the new regulatory state": I dropped this term once more. It is now time to pay some attention to it; as it happens my *coming out* runs very much parallel to theories revolving around this concept.

[3] G.J.Vonk, 'De publieke taak in het stelsel van sociale zekerheid' in: *De publieke taak,* J.W. Sap, B.P. Vermeulen en C.M. Zoethout (eds.), Deventer, 2003,165-184

But this is no easy task. The regulatory state is in itself an elusive concept[4], making sense of the new one is nigh impossible! Let me try to present the picture as simply as possible, happily stealing from the excellent account of our reviewer Jason Solomon, referred to earlier.

In Europe we refer to the regulatory state to denote the change from a government which is the direct provider of services into a government which interferes indirectly in the economy and society. Not rowing but steering. The traditional means for the state to steer are regulation, supervision and enforcement. It is the state that sets rules which must then be complied with by private actors. The state enforces these rules by inspection and imposing sanctions in case of non compliance. This Solomon refers to as the command and control model.

But this model has come under attack as well. Part of the criticism deals with the inefficiency of the rulemaking process. In a world of uncertainty, legislatures and agencies are unable to predict what the best rules must be and the mechanisms for adjusting the rules are lacking. Furthermore, compliance levels are low. Many case studies point out that, without the acceptance of the parties involved, regulation is ineffective. Also, scarce state resources mean that agencies are unable to sufficiently help private actors to comply, to enforce the law, or to monitor and update rules in the light of experience.

According to Solomon, the new regulatory state arises out of the critique of the command and control model. Instead a new model of collaborative governance is advocated, where public authorities and private actors work together to define and revise standards. The public authorities act to help private actors learn from each other about best practices and ensure transparency and public participation in problem solving. In such a model public and private actors interact in increasingly complex and collaborative ways to address problems of public policy. And they do so not only using the formal law, but also by

[4] There is vast body of literature on the regulatory state. For an overview see Michael Moran, 'Review article, understanding the regulatory state, B.J.Pol.S., 2002, 391-411.

developing new instruments: soft law, non-binding covenants, behavioural codes, positive feedback loops and public success ratings and pubic shaming.

In the ideal of the new regulatory state law should facilitate an *autopoietic*, (or self generating) system of rule making. It does not dictate the behaviour of others, but helps others to set rules themselves which are best fitted to their needs. Public goals and private interests can be reconciled when both private actors and public agencies work together in de process of rule making.

4. Criticizing the new regulatory state

I now move on to my last strand: criticizing the new regulatory state. Surprisingly, in literature the concept of the new regulatory state does not meet much opposition, at least up to the best of my knowledge. If anything, it is the traditional legal approach that is criticized because it does not show enough flexibility and understanding to incorporate new forms of governance into its realm. Thus, for example in the book edited by the De Búrca and Scott one author voices his disappointment about the attitude of the American Courts which apparently struck down an innovative occupational health-and-safety program because it did not comply with formal rulemaking requirements. [5]

In order to find legal criticism of the concept of the new regulatory state I have to stay closer to home where some lawyers do raise concerns. Reference can be made for example to Sjoerd Zijlstra, professor of constitutional and administrative law at the Vrije Universiteit in Amsterdam, a self proclaimed 'binary' thinker, i.e. public is public and private is private. He once confided to me that the purpose of the law is to demarcate responsibilities and competences and clear procedures. These may lay dormant in times of prosperity and harmony. But in times of conflict and crisis the law must show what it is worth, making clear who is accountable and what rules should be applied to re-

[5] Orly Lober, 'Governing occupational safety in the United States' in: *Law and the new governance in the EU and the US*, Gráinne de Búrca and Joanna Scott (eds.) 269-292, 279-280.

establish order. Mixing private and public responsibilities in the new regulatory state undermines this function of the law.

In a contribution in 2003 Zijlstra elaborated on this theme in reaction to a report published by the Dutch Scientific Council for Government Policy on the rule of law in the Netherlands.[6] According to this report the Dutch legal system is out of balance because public authorities are bound by all sorts of constraints ensuing from the democratic legal order, such as the general principles of public governance and democratic accountability, while private actors are merely bound by the general laws. Therefore the report recommends that also private actors should take on public responsibilities. Zijlstra disagrees. According to him the disbalance is the essence of our democratic society; the citizen is free, but for the restrictions imposed by law. If you belong to government your action must be governed by public law and if you do not...then not. Therefore, in Zijlstra's view hybrid public/private organizations are a curse; they will only lead to misunderstandings and chaos.

In my eyes this critical point of view is to be taken seriously. In a more recent report, the Dutch scientific council has analyzed the privatization measures which the Dutch government has carried through over the last decades in the field of infrastructure of drinking water, communication, energy and transport.[7] The report observes that in these areas the state has relinquished direct responsibility for the operation of infrastructures to a multitude of actors. As a result it is no longer clear who is responsible for long term public interests such as environmental protection and qualitative investments. According to the report, a return to direct state intervention in investment decisions is no longer considered a realistic or fruitful option. This may be understandable but the alternative medicine that is proposed by the scientific council is rather vague. For example it proposes an "evolution of sectoral roadmaps". These

[6] S.E. Zijlstra 'publieke taak' en democratische rechtstaat' in: *De publieke taak,* J.W. Sap, B.P. Vermeulen en C.M. Zoethout (eds.), Deventer, 2003, 69-76.

[7] Scientific council for government policy, *Infrastructures: time to invest,* The Hague, 2008.

> should be conceived as a form of strategic dialogue and partnership between the relevant stakeholders. These strategies could be prepared in the first instance by a panel of independent advisors who would in turn draw on the expertise of a wide range of stakeholders, and who would provide informed and non partisan advice on the objectives to be met and the options for meeting them.

Another quote from the report:

> Combined action at all different stages of the process of designing and operationalizing a strategic perspective will provide greater certainty and clarity for the various actors involved with the infrastructures and engenders trust and commitment. Furthermore, the process of combining or re-connecting encourages and improves coordination across and between the different splintered arenas, creating openings for an alignment of competing interests".[8]

How much vaguer can it get. Despite all the good intentions, it all sounds so very much, well… like the new regulatory state. One wonders whether the report would have gained strength if it would have argued in favour of simple procedures and a more clear cut delineation between private roles and public responsibilities.

Back to the credit crunch. It seems to me that a parallel can be drawn between the debate on the governance of infrastructures and the financial markets. Unclear procedures and lack of state supervision resulted in the system coming to an abrupt standstill with no one to be held accountable. And eventually, it is the state that has to assume responsibility, breaking into the intricate governance model with its big boots of direct intervention. Let us hope that in the area of infrastructure we will not allow such a crisis to emerge before we come to our senses. It is not without reason that Holland keeps its dikes firmly under public control. After all we are below sea level and hence we cannot afford much experimenting with forms of new governance in the area of our sea defences.

I am not advocating an end to the new regulatory state. Of course it is still a viable concept. But I think the system should not be allowed to become too complicated making

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[8] Scientific council for government policy, *Infrastructures: time to invest,* The Hague, 2008, 40

it unmanageable and ineffective. Perhaps the relationship between law and governance should be reconsidered once more. In vital sectors, not too much substantive law should be allowed to leak away from the formal legal domain (and its command and control model) into alternative constructions set up by the local actors involved. And the law itself should provide clear procedures and protect the distinction between public functions and private interests, so as to create clarity as to the division of responsibilities.

5. Final remark

We, scholars of the law can offer a small contribution to the improvement of the regulatory state. It is with great pride that I am able to announce the initiative of the Groningen Law Faculty to set up an institute on public governance and private interests. The focus of this institute is the regulatory state. It will bring together specialist in the Netherlands and abroad to create a centre of excellence in which academics will be given the freedom, time and money to carry out independent research. The University has offered an initial financial injection of 5 million euros, but we hope that we can soon align ourselves with other universities inside and outside the Netherlands. Our network conference of the last two days is just a foretaste of what is about to come. I thank all of you very much for your contributions. You have done excellent work. I hope the Groningen Institute will provide a welcome platform upon which we can meet again in the future.