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REGULATORY GOVERNANCE AND
THE CHALLENGE OF CONSTITUTIONALISM

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Regulatory Governance and the Challenge of Constitutionalism

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Abstract

The late twentieth century witnessed significant shifts in the institutions and processes of governance in most members states of the OECD, as direct provision (sometimes characterised as welfare state governance) was, to some degree, displaced by the rise of the regulatory state. Changes in the nature of state intervention have been accompanied also by fundamental challenges to traditional conceptions of the centrality of the nation state as regards its dominance of key resources (notably taxation and capacities for coercion) and for the maintenance of the rule of law and democracy, as transnational and non-state power have assumed greater significance. In this paper I assess both narrow and broad versions of the challenge presented to the values of constitutionalism by regulatory governance. The narrow constitutionalist critique locates the problem of regulatory governance with the delegation of governmental power to regulatory agencies. A broader constitutionalist critique looks beyond delegation to other organs of the state, and notes that the de-centring of regulatory governance has increasingly implicated both non-state and supranational governmental bodies in regulatory tasks through implicit and explicit delegation and through the assumption of regulatory powers with little or no state involvement. I suggest that one response to the broad critique is to institutionalise broader modes of control and accountability which are best able to match the governance powers which are targeted.

Keywords

Regulation; Constitutionalism; Governance; Private Regulation; Rule of Law; Networks
1. Introduction*

The late twentieth century witnessed significant shifts in the institutions and processes of governance in most members states of the OECD, as direct provision (sometimes characterised as welfare state governance) was, to some degree, displaced by the rise of the regulatory state. 1 Changes in the nature of state intervention have been accompanied also by fundamental challenges to traditional conceptions of the centrality of the nation state as regards its dominance of key resources (notably taxation and capacities for coercion) and for the maintenance of the rule of law and democracy, as transnational and non-state power have assumed greater significance. 2

The shift towards regulatory styles of governance, associated with the creation of independent agencies and greater deployment of legal rules, creates the risk of a high-handed state apparatus, with broad discretion and concentrated power. The regulatory state presents rather obvious difficulties for constitutional doctrines, and in particular the tensions between effective and instrumental regulatory governance, on the one hand, and demands for accountability and respect for process and rights within constitutionalism on the other. 3 Constitutionalism is a term which seeks to capture the idea that public power is or should be limited and subject to some higher form of control by reference to law. This idea of limited public power is applied to both legislative and executive branches of government. 4 In this chapter I assess both narrow and broad versions of the challenge presented to the values of constitutionalism by regulatory governance.

The narrow constitutionalist critique locates the problem of regulatory governance with the delegation of governmental power to regulatory agencies. Such delegations may be quite extensive and arguably undermine the effectiveness of the limitations placed on legislative and executive power. This challenge has been particularly significant in the United States, where there has been a longer history of extensive delegation to regulatory agencies, but arguably has taken on wider significance as the trend towards delegation to regulatory agencies has spread to other OECD members since the 1980s. A broader constitutionalist critique looks beyond delegation to other organs of the state, and notes that the de-centring of regulatory governance has increasingly implicated both non-state and supranational governmental bodies in regulatory tasks through implicit and explicit delegation and through the assumption of regulatory powers with little or no state involvement. 5

One response to the diffusion of regulatory power is to seek the application of traditional modes of control and accountability, seeking their extension beyond state actors to those who were found to wield power. I do not suggest that this is always inappropriate, but, as a comprehensive solution to the

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* A later version of this paper will be appear in Dawn Oliver, Tony Prosser and Richard Rawlings (eds) In the Regulatory Laboratory: Law, Governance and the Constitution to be published by Oxford University Press. The paper was originally presented at a conference entitled The Regulatory State: Constitutional Implications organised by the United Kingdom Constitutional Law Group and the International Association for Constitutional Law and held in London in November 2008. I am grateful to participants for comments.


adaptation of constitutionalism to regulatory governance it is likely to be incomplete. I suggest in this chapter that the alternative is to recognise diffusion not only in actors but also in modes of regulatory governance. Such a move recognises a broader shift in constitutionalism from its liberal legal underpinnings to a version which emphasises legal pluralism as a central characteristic of globalization. To follow this logic suggests seeking to institutionalise broader modes of control and accountability which are best able to match the governance powers which are targeted. Such an approach is suggestive of a regulatory critique of constitutionalism in which greater recognition is accorded to the variety of ways in which power is structured and limited, going beyond relatively formal legal conceptions of constitutional controls.

2. Constitutionalism

A constitution is the constellation of norms and practices, through which certain principles of governance are given effect in terms both of the relationship between the constitutional actors, and between those actors and citizens. It allocates powers to the various organs of the state and expresses the conditions for their exercise and thus, implicitly, at least, also their limits. Embracing ideas of constitutionalism responds to the recognition of the dispersal of constitutionally relevant activities around the organs of the state and argues for the regulation of public power. A central aspect of the idea of limited power is that the three key state capacities – legislative, executive and judicial - should be exercised in institutionally distinct organs of the state, each of which has a counterbalancing effect on the powers held by the others. Constitutionalism, though not admitting of any agreed definition, extends beyond the idea that government should be subject to law (‘the rule of law doctrine’) to hold that the legislature itself should be constrained in what it may legislate for by higher constitutional norms. Amongst legal scholars the desiderata of constitutionalism extend to defining the limits on executive and legislative branches of government in terms that are ‘legally binding’. In constitutional discourse in the United Kingdom the commitment to this form of legal constitutionalism is at odds with the idea that the limits on the capacity of the legislature are elements of a political rather than a legal constitution. In the United States, by contrast, constitutional review of legislative activity is a long established aspect of democratic theory and practice.

For a regulatory scholar the presence or absence of legal norms governing legislative acts is only a beginning and not an end to the inquiry, since the presence of legal norms does not tell us whether or not and how such norms are monitored and enforced. Even within regimes which empower courts to strike down legislation which breaches terms of a written constitution the extent of judicial oversight over legislative acts is partial and sporadic, rather than systematic. It is arguable that mechanisms of non-judicial review, for example engaging legislative committees in oversight and application of

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8 Samuel E Finer, Vernon Bogdanor and Bernard Rudden, Comparing Constitutions (1995): 1
10 Ibid.: 455.
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constitutional principles, might provide for more systematic oversight. Consequently the question whether the limits over legislative power are exercised politically and/or legally is less important than the attempt to understand the nature and extent of constitutional monitoring of public power or legislative and other kinds. This insight is important in evaluating the constitutional standing not only of core state activities, but also of more diffuse regulatory governance regimes.

If it is correct that constitutionalism involves a commitment to effectively limit the exercise of legislative and executive power, by reference to some higher norms and for the purpose of upholding democratic governance, then it is of considerable importance either that such executive and legislative power is not delegated or, where it is delegated, it is subjected to similar controls. Accordingly, from the perspective of constitutionalism, delegation is the central problem associated with contemporary regulatory governance. The nature and extent of delegation one perceives depends centrally on how one conceives regulatory governance. A classical and state-centred view of regulation presents a problem of overseeing and controlling power delegated to regulatory agencies. I refer to this as the narrow critique of regulatory governance. Practice and scholarship have moved beyond the state as the only, and in some cases the primary, focus of regulatory governance. Decentred conceptions of regulation in which non-state and supranational actors play central or substantial roles provide a fresh set of constitutional challenges which I discuss in the section below on the broad critique.

3. The Narrow Critique of Regulatory Governance

Classical separation of powers doctrines refer to three basic branches of the state – the legislature, the executive and the judiciary - and hold, to varying degrees, that it is desirable for there to be a degree of separation between them, such that each may hold the others in check. Regulation is frequently conceived of ‘as sustained and focused control exercised by a public agency over activities that are valued by a community’. To the extent that regulation comprises the activities of regulatory agencies it presents a double constitutional problem. First, agency regulation involves a degree of delegation by the legislature of executive power beyond the politically accountable government departments which comprise the core executive. Processes of agencification are not, of course, limited to regulatory governance, and have been seen also in many countries in operational areas such as the provision of health and welfare. Second the powers delegated to agencies, particularly in the United States, tend to extend beyond the traditional administrative powers of the executive to include also rule making and adjudication, functions normally reserved to the legislature and the judiciary respectively. While regulation presents as a problem to constitutionalism, ideas of constitutionalism also act as a restraint on such delegations. Many and perhaps most states only permit very limited delegation of rule making powers, if at all, and limit the degree to which agencies can apply sanctions to those they oversee without application to a court. Accordingly the primary focus of the narrow critique is on practice in the United States where tensions over the emergence of the independent regulatory agency model have resulted in significant constraints on the exercise of apparently wide-ranging powers.

Amongst the earliest of the United States federal agencies was the Interstate Commerce Commission, established in 1888 to regulate trade within the ‘single market’ of the United States. The ICC was established originally on a judicial model, with central functions linked to adjudication of disputes. The early history of the ICC is also the history of the constitutional battle over the expansion of the adjudicatory model of regulatory governance to one that progressively took on the functions of rule making and more systematic monitoring of markets than the reactive image of adjudication might

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The embryonic model of agency-based regulatory governance was firmly established by the time that a number of new federal regulatory agencies were created during the New Deal era, and the persistence of the model beyond the period of the last great depression, was, in a sense confirmed by the introduction of the Administrative Procedure Act in 1946. US law adapted itself to the reality of a significant concentration of legislative, executive and judicial authority in the agency form. Writing of the Canadian agencies which mimicked the US form, John Willis famously described these agencies as ‘governments in miniature’. The challenge to constitutionalism presented by such agencies is rather clear. The Canadians have retreated from such extensive allocation of powers to agencies in recent years.

I have argued previously that the North American experience, both in terms of allocation of powers to agencies, and their constraint by procedural rules within a culture that tolerates and even promotes ‘adversarial legalism’, is atypical of regulatory governance models more generally – an example of American exceptionalism. Notwithstanding the significant constitutional constraints on the emulation of the US experience, arguments for the expansion of the regulatory agency model to other jurisdictions are commonly made. Two principal arguments are put forward. First, it is argued that agencies may develop a focus and expertise which enables the execution of governmental tasks more effectively, and second that the independence and expertise of such agencies insulates them from political decision making thereby increasing the commitment and credibility of regulatory policies, and thus promoting investment in the regulated sector. The second argument is of particular importance in respect of network industries where investment costs are high, but may also be adapted to cases where confidence in governmental action is limited because of the power of sectional interests in influencing government. The hold of the agricultural industry over governments may, for example, provide a good argument for independent regulation of food safety. However strong the arguments in favour of independent regulation may be, the giving away of legislative and executive powers by parliaments and governments is far from straightforward in many government systems. Thus while regulatory agencies have proliferated over recent years through most of the OECD member states, it is frequently with limited independent powers to make and enforce rules.

Crisis of the BSE, Enron, and financial types inevitably stimulate responses along the lines that we need more stringent state regulation. Such incidents are said to increase the appetite for ‘blame and punishment’. Attempts to revive ‘command and control’ regulation in situations of crisis are more or less inevitable, from a political perspective. Whilst understandable, a more appropriate response to

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such crises might be to recognise the limited capacity of governments to control everything. The paradox of regulatory agencies in many jurisdictions is that the implicit or explicit application of constitutional restrictions means they frequently have too little power to exert control, but too much power to be legitimate. These dilemmas of legitimacy and effectiveness provide part of the explanation for a new emphasis, both in practice and in scholarly analysis, of ‘decentred regulation’ which moves us beyond national state agencies to consider the practices of supranational and non-state organisations. Such practices provide a rather greater challenge to constitutional analyses of public power, which I address in the next section of this chapter.

4. The Broad Critique of Regulatory Governance

The ‘rise of the regulatory state’ has powerfully captured the idea of a shift in modes of governance away from the direct provision model of the welfare state to arms-length oversight by government of other providers. A principal emphasis of the regulatory state analysis has been on the growth in regulatory agencies. But recent scholarship has questioned some aspects of the regulatory state image, preferring to conceive of regulatory governance in a manner which is highly fragmented, both within the state, and beyond the state with substantial involvement of supranational and non-state organisations at every stage, including the making, monitoring and enforcement of norms. In a very influential article Julia Black characterised this process as the ‘decentring’ of regulatory governance. Clifford Shearing and co-authors have discussed the phenomenon in terms of ‘nodal governance’. In my own, preliminary thoughts on the issue, I have written of the ‘post-regulatory state’. I now think the concept of ‘regulatory capitalism’ advanced by David Levi-Faur, Jacint Jordana and John Braithwaite, may better capture developments. The concept of regulatory capitalism embraces the idea that there may be growth in both state regulation and growth in non-state regulation – a simultaneous re-centring and de-centring – a phenomenon identified recently in the UK.

In some ways this diffuse and fragmented image of regulatory governance presents more of a challenge to ideas of constitutionalism than a highly centralised accretion of regulatory power. In particular, it works with a more pluralized conception of power than that which is familiar within constitutional discussions of state sovereignty. Whereas 18th and 19th century constitutional debates

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were animated by a concern with ‘disciplining repressive political power by law, the point today is to discipline quite different social dynamics’. 35

The key point underlying John Braithwaite’s claim that contemporary governance arrangements are best characterised as ‘regulatory capitalism’ is that non-state regulatory governance has grown in significance more rapidly than have regulatory agencies spread. 36 Such a change does not necessarily reduce the significance of the state, since it may have a strong presence or ‘hidden paw’ within private regulatory regimes. 37 A significant aspect of this fragmentation is attributable to supranational governance bodies, both governmental and non-governmental. Alongside ministries and agencies, we have the familiar self-regulatory bodies, but also standards bodies, national and international, general and sectoral. Businesses themselves are important in regulatory regimes, not only because they have (sometimes limited) capacities to control behaviour within their own organisations, but also because they can regulate the behaviour of others. A key instrument is the supply chain contract, through which not only can firms set standards, they can also set down the instruments of monitoring and enforcement, which may involve third parties to certify or audit compliance with standards. 38

A particular form of third party regulation invokes the gatekeeping capacity of certain actors, who frequently have the power, but perhaps not the incentive, to regulate others. 39 Faced with the apparently intractable problem of enforcing rules against internet gaming in New York State, the then Attorney General Elliot Spitzer, finding it almost impossible to enforce criminal law against businesses with their servers and financial interests in Antigua and other off-shore locations, caajoled the leading banks to use their capacity to block internet gaming transactions on credit cards they had issued. 40 Airlines and insurance companies have similarly had their regulatory capacity harnessed by government, in the enforcement of immigration, 41 and intentional oil pollution, 42 respectively. Non-governmental organisations also increasingly use their capacity to regulate for setting and/or enforcing standards. Businesses and NGOs can sometimes be cast as regulators over government. 43

It is not just the actors in contemporary regulatory governance who are diverse, it is also the ways of governing. Self-regulatory regimes can, in many ways, mimic public regulatory regime with enforceable rules (deriving authority from statutory delegation or from contracts between the parties) and mechanisms for monitoring and formal enforcement. But many regimes of both public and private regulatory governance deviate markedly from such a classical model of hierarchical regulation. Even with classical regulatory agencies empirical research suggests that hierarchical enforcement is frequently the exception rather than the rule. Education, advice and warnings are frequently judged

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42 Ronald B. Mitchell, Intentional Oil Pollution at Sea (1994).
sufficient to encourage businesses to modify their behaviour. The effective implementation of technical standards is frequently more a matter of rational market behaviour of actors than top-down enforcement. And whilst the opposition between hierarchies and markets as basic governance choices has long been observed, significant attention is now being paid to the importance of a third organising mode based in communities and networks. It has been widely observed that the governance of the European Union has made a significant turn away from the ‘classic community method’ based in hierarchy, towards a more networked form of governance associated with the Open Method of Coordination, and regulatory networks of the kind that shape key aspects of regulation in member states affecting competition, energy, communications and financial markets.

One solution to the constitutional problems surrounding diffuse regulatory governance is to seek to apply traditional controls over all regulatory actors, as if they were public agencies – judicial review, parliamentary accountability, ombudsman complaints, and so on. One approach to the dilemma involves a search for common values across public and private law, suggesting that private law mechanisms should and/or do involve the application of similar principles to those exercising power as would public law mechanisms. The related phenomenon of ‘publicization of private law’ involves the development of mechanisms and norms through which private actors are enrolled in the delivery of public functions. Something of this approach can be detected in the Global Administrative Law movement, which seeks to identify emergent common principles and practices in structuring the decision making of supranational and non-governmental administrative and quasi-administrative power. These emergent principles call for transparency and participation in decision making, reasoned decisions, compliance with principles of legality and provision for review. In her elaboration of what might be connoted by the Global Administrative Law, Harlow suggests that it might extend well beyond the adoption of procedural principles to encompass the values of the rule of law, good governance and human rights, lending it a substantive dimension resonant as much with constitutional as with administrative law norms. But, as she notes, there is an absence of structures to support the operationalization of such principles, and a likelihood that efforts to create such structures would result in fragmentation.

While fragmentation in regulatory capacity and oversight is a problem, it might also be a solution. The separation of powers is a standard constitutional solution to the risks of governmental power and can be adapted to broader fragmentation than simply that between executive, legislature and

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46 Graeme F. Thompson, Between Markets and Hierarchies: The Logic and Limits of Network Forms of Organization (2003).
48 Hugh Collins, Regulating Contracts (1999); Dawn Oliver, Common Values and the Public-Private Divide (1999).
52 Ibid.: 211.
From this perspective it is the excessive concentration of power, rather than diffusion, which is a problem. An alternative way of expressing this insight is to highlight the variety of modes of governance within regulatory regimes and, following insights of the cybernetics, the science of control systems, and in particular the law of requisite variety, seek to institutionalise broader modes of control and accountability which are best able to match the governance powers which are targeted. The extension of the hierarchical model of administrative law, seen from this perspective, provides only one possible set of mechanisms and is likely to be incomplete by itself. A broader approach seeks a wider range of institutionalised mechanisms equivalent to constitutional controls.

5. The Diffuse Constitutionalization of Fragmented Regulatory Governance

Constitutions, conceived of as the living procedures through which powers are allocated and controlled, whether expressed in law, convention, practice or a combination thereof, are at base institutionalized mechanisms for addressing the problem of governance power. Such institutionalized mechanisms include the scrutinizing role of legislatures over the executive, alongside the legislative power, the potential for judicial review of executive and legislative powers, and the institutionalization of other mechanisms of oversight, for example through an expanded conception of public sector audit and the development of novel grievance handling mechanisms. Though legislation which embraces conceptions of human rights may be adopted through ordinary legislative processes rather than constitutional amendment, nevertheless it forms part of system for allocating and controlling powers. Equally the routinization within government of new mechanisms for monitoring and controlling such things as public expenditure and the promulgation of new regulatory rules also have the potential to fundamentally affect the stock of constitutional controls over the exercise of power. Similar processes of routinization through networks and establishment of expert fora, distinct from the operation of related judicial fora, can be seen in supranational organisations such as the World Trade Organisation.

Although the majority of jurisdictions have constitutional documents which allocate and regulate governmental power it is frequently misleading to restrict the concept of constitution to those instruments because an array of accompanying norms and processes tend to spring up within constitutional practice which, together with the foundational documents, comprise the ‘living constitution’. Indeed these additional elements of a living constitution are not restricted to judicial pronouncements interpreting constitutional texts, but extend also to actions and processes which engage the legislative and executive branches of government.

60 Ibid.: 231-239.
Accordingly one way to approach the potential for reconciling regulatory governance with constitutionalism is to identify examples where institutionalized solutions have been developed. In this context institutionalization refers to implicit or explicit attempts to couple two spheres of meaning, two different ways of viewing the world. I attempt this task in the following sections, addressing examples of hierarchical, competitive and networked governance, but without, at this stage, offering a comprehensive theory.

5.1 Institutionalising Hierarchy

The classic form of regulatory governance involves the application of hierarchical power – the making of regulatory rules, exercise of powers to monitor for compliance and enforcement action against those found to be in breach. Regulation, broadly speaking, is an instrumental form of law concerned with securing particular objectives. Thus it may be efficient to delegate powers to agencies, make rules quickly, to apply them to a subsection of the community, rather than universally, and to enforce rules in a differential way, reserving formal legal enforcement for a small minority of cases and using less stringent methods such as education and advice in the majority. But such processes might offend principles concerned with the universal application of law, and rights of those subject to regulation, for example a right to be heard before their economic interests are adversely affected by a new rule, and an expectation that all firms should be treated equally before the law. The discourse and practice of rights is not concerned with instrumental objectives, but rather the protection of rights as a value in itself.

In many instances the tension between the instrumental approach of regulation and respect for rights is recognised through the institutionalisation of protections of rights as an accompaniment to the enhancement of regulatory powers. Thus the expansion of the scope and powers of regulatory agencies in the US in the New Deal era was balanced by the passage of the Administrative Procedure Act in 1946. Recent measures in the UK which have extended powers to make rules and to apply sanctions directly against businesses, ‘the new punitive regulation’, have been accompanied by the establishment of new tribunals. For example, the Competition Appeal Tribunal was established in 2003, to hear appeals within a regime where the regulators (both general competition and sectoral) are able to apply sanctions directly against firms without recourse to a court. Similarly, the Financial Services and Markets Tribunal was established in 2000 at a time when the new regulator, the Financial Services Authority, was established with powers to apply financial penalties for market abuse directly.

Such institutionalised mechanisms for balancing the delegated power and discretion of agencies make such governance forms relatively unproblematic from the perspective of constitutionalism (though we might debate the appropriate intensity of such mechanisms), particularly where practices are consistent with the expectations of the parties affected. We should note also that in the UK there has been a trend towards tighter managerial control over agency enforcement through the use of soft

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65 Ian Ayres and John Braithwaite, Responsive Regulation: Transcending the Deregulation Debate (1992).
law instruments. More challenging is the use of other legal forms, such as contracts, for the exercise of regulatory power, whether in the context of public procurement or regulation through contracts (for example in the case of contracted out prisons), or private governance through supply chain contracts. Such contracts are typically bilateral and opaque and, because of the uneven economic power, difficult for one party to challenge.

A key example of contract-based governance has attracted particular controversy. What should we do, in constitutional terms, about self-regulation? The problem has been expressed in terms of a stark choice for the courts between the application of public law principles, upholding the rights of persons subject to the decisions of self-regulatory associations, and ‘respect [for] the autonomy of the association to make and interpret its own rules, or to determine its own membership.’ The ‘constitutionalization’ of self-regulation may be addressed through the development of a theory of judicial review over self-regulatory bodies. It is telling that few common law jurisdictions have been as bold in extending principles of judicial review to self-regulatory bodies as England and Wales. The all or nothing approach which looks only to judicial review is limited because of its emphasis on finding a distinction between public (reviewable) and private (autonomous) power. Just because an organisation is immune from judicial review does not mean it is autonomous.

Rather than suppose that even adapted versions of standard constitutional doctrines can be applied to the fragmented world of regulation represented by contractual governance, it may be more productive to reconceptualise the challenge of constitutionalism as involving the recognition of alternatives to orthodox constitutionalism in defining the limits and acceptability of the conduct of regulatory governance. Such a focus additionally takes us beyond a narrow constitutional concern with relationships between state and (real and corporate) citizens to consider wider issues of allocation and control of power, whether publicly or privately exercised. Such a focus invokes private capacity not only in the exercise but also the oversight of public functions. Thus, although regulation by contract is a hierarchical mode of control, its oversight might be institutionalised through competitive or network processes rather than a hierarchical mode in some cases, discussed in the next two sections.

5.2 Institutionalizing Competitive Processes

Competition and rivalry constitute a basic form of control fundamentally different from the application of law and hierarchy. This is not to deny, of course, that there is a legal and constitutional underpinning to the operation of markets, but rather to suggest that competitive processes which exert control and accountability functions are analytically distinct from hierarchical constitutional controls. To the extent that regulatory tasks are undertaken through processes of competition rather than legal control this raises constitutional questions of oversight of and accountability for the power exercised within such regimes. In some domains governments attempt to exercise a clear choice that objectives are to be delivered through competition rather than regulation. Processes of liberalization in the utilities sectors in many countries have raised persistent questions about whether it is better to regulate such matters as access to networks and prices, or leave market actors to negotiate and determine such matters by reference to market norms, with an expectation that the market might find

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73 Ibid.: 32.
alternative solution to those envisaged by regulators (for example developing new infrastructure as an alternative to negotiating over access).  

Leaving issues of allocation and pricing of key resources to markets can, of course, be uncomfortable for governments, which find it impossible to be entirely detached from such matters as rapid increase in energy prices, or threats to security of supply caused by the stripping out of redundant capacity by firms seeking to maximise revenues. And it is not necessarily the case that an absence of regulatory oversight means noone is in charge. An official report in New Zealand concluded that one consequence of seeking to liberalise the telecommunications market in the early 1990s without establishing a regulatory agency to oversee the process was that the dominant incumbent telecoms operator had become the *de facto* regulator for the sector, its decisions determining the terms and conditions on which the whole market operated.  

A key question, relating to the theme of constitutionalism is whether competitive processes can substitute for some or all of the requirements associated with more orthodox constitutionalism. Advocates of regulatory competition suggest that the mobility of capital may exert competitive pressures over governmental activities such as local taxation. Applied to regulatory regimes, operating at national level but in transnational settings, it is claimed that such regulatory competition might create a downward pull on regulatory standards, exerting a quasi-constitutional function in inhibiting governments from excessive regulation as it would risk the flight of capital to other states. The nature and intensity of such controls is, of course, an empirical question for investigation within particular regimes.

Could there be a similar quasi-constitutional dimension to the operation of competitive pressures more generally? A key aspect to regulatory competition over states is that the downward pull of competitive pressures is balanced by the upward pull of electoral politics. Thus, for example, the abandonment of employment protection measures might be a good thing from the perspective of promoting inward direct investment, but be politically unthinkable for a government seeking to be re-elected in future years. Is there any equivalent upward pull in the competitive processes of markets? A partial answer to that question lies in asking why many firms act more responsibly in areas such as consumer and environmental protection than they are required to by law. The takeoff of regimes of corporate social responsibility, led by firms and associations of firms, is an institutionalised version of this. Such developments may be partly explained by pure market concerns with reputation. Reputation is important to the capacity to operate in very diverse markets ranging between investment banking, to the supply of white goods and groceries to consumers. No doubt there are markets where reputation is not important, but where it is then, arguably it exerts an upwards pull counterbalancing the competitive pressures to reduce costs and quality.

How might such an argument be relevant to regulation? Arguably there are some important regulatory functions which are undertaken by market actors under conditions where competition is the main mechanism of oversight and control. Amongst the questions still being asked amid the wreckage of the financial crisis is whether the implicit delegation to markets for the control and oversight of credit rating agencies was a cause or accelerant in some of the difficulties. Regulators and businesses alike are dependent on the assessments made by credit rating agencies for issuers of credit instruments as to their creditworthiness to determine risk and therefore both willingness to lend and appropriate

terms and, in the case of regulators, the net capital reserve requirements of banks. It has been argued that the activities of credit rating agencies provide a key example of market based coordination through standardisation.\textsuperscript{83} Notwithstanding their importance, which extends also to reporting on sovereign debt, there has been little regulatory oversight over credit rating agencies other than a degree of vetting of agencies where reports are relied on for regulatory purposes. This is not to say that these organisations have not been subject to control. The agencies face the normal pressures to reduce costs and make profits. There is also a strong reputational aspect to their work.\textsuperscript{84} Were experience to show that their ratings were unreliable, those ratings would be reduced in value for those relying on them and, over time, the agency involved would lose business as its clients found that lenders were unwilling to rely on the judgments. Such control has not prevented catastrophic failures (which have resulted in proposals for new hierarchical oversight\textsuperscript{85}). A central problem with the behaviour of the agencies, identified amongst the causes of the global financial crisis, was the excessive pull of client banks with capacity to shop around for high ratings, as against the more diffuse reputational effects associated with putting forward reliable ratings.\textsuperscript{86}

Key constitutional issues concerning such market coordination for standards is what mechanisms exist to hold credit rating agencies accountable for errors, how transparent are such errors and how does the knowledge of such errors feed back into the system to improve it.\textsuperscript{87} It has been argued that the increasing global power of agencies in the market place has not been accompanied by increasing accountability. One dimension to this is that there is limited competition in the market and, the recognition of a limited number of agencies in the market for regulatory purposes may have further reduced competition – the very force on which the market is dependent for oversight. Additionally the agencies do not accept legal liability for their ratings – they issue them as a guide to risk only.\textsuperscript{88} It remains an open question whether the reputational pull of the market is sufficient to counter these weaknesses.

If credit rating agencies demonstrate weaknesses in institutionalization, then the world of technical standards provides examples of highly institutionalized communities within broad market settings. Schepel’s major study of such processes led him to conclude that ‘[p]rivate standardisation has assimilated the canons of administrative rulemaking to such an extent that it is hard to find a difference between its procedures and the procedures that sanction delegations of regulatory power to public agencies, other than that of a formal link to public power.’\textsuperscript{89} Such examples are indicative of a more hybrid alternative to competitive pressures for control over market actors.

Less well developed examples of institutionalization are found in the emergence of non-state market-driven (NSMD) governance in some environmental domains where more networked governance is overlaid on the market. In the case of the Forest Stewardship Council (FSC) a network of NGOs and others including industry and governmental representatives constituted a network which


\textsuperscript{84} Fabian Dittrich \textit{The Credit Rating Industry: Regulation and Competition} 2007).


\textsuperscript{88} Ibid.

sought to define standards for sustainability in logging. The mechanisms through which FSC standards have been taken up have been linked to the marketplace, and in particular tactics such as protests designed to persuade major retailers to require FSC compliance for wood products sold in their stores. The main motivation for the retailers to use their contractual power in this way is reputational, exploiting the ideas that a significant proportion of consumers are exhibiting ‘preferences for processes’ rather than for quality and price on their own. The emergence of the fair trade movement appears to have similar origins.

The emergence of the FSC as a powerful environmental regulator clearly raises questions about accountability. Arguably the FSC is subject to a form of complex market-based accountability. Faced with reputational issues concerning sustainability of the wood products it sells a retailer has choices to do nothing about it, to learn about the issues and set its own standards, or to adopt a standard set by someone else. The FSC is one of a number of competing regimes in the area of sustainability of logging. Accordingly the FSC is subject to the pull of competition between a variety of alternatives, with the quest for reputation pulling standards upwards and some downward pull because of the choices retailers have. The reputational dimension is very important. If the standards developed turned out to be poor, or if the monitoring of compliance turned out to be inadequate, the FSC regime would be threatened, but the credibility of similar regimes involving labelling of certified processes might also be damaged.

5.3 Institutionalizing Networked Governance

Whilst the contrasting of markets and hierarchies as forms of governance is well established in the literature, the emphasis of more recent research has been on exploring the significance of networks and communities in regulatory governance. Networks are characterised by voluntary participation which frequently transcends both state/non-state distinctions and national boundaries. Research on governance through networks has highlighted the significance of epistemic communities in shaping what is knowable and doable by constituent members, and has demonstrated the importance of less hierarchical modes of governance both in formal transnational government arrangements, such as the EU and in non-governmental activities of NGOs, trade associations and others such as standardisation bodies. The arrangements by which actors in such networks and communities hold each other to account and exert control over one another have been described in terms of the potential of ‘societal constitutionalism’.

The constitutional challenge associated with such network arrangements lies in their capacity to get things done outside the structures of formal legal governance through generation of norms, codes, guidance and monitoring and behavioural modification mechanisms such as surveillance, benchmarking, etc. In some instances such non-legal norms are adopted as de facto standards in markets, and in other instances they may crystallise into legal rules. Accordingly there is a continuum

91 Errol Meidinger, ‘Forest Certification as a Global Civil Society Regulatory Institution’ in Errol Meidinger, Chris Elliott and Gerhard Oesten (eds), Social and Political Dimensions of Forest Certification (2003): 280.
94 Graeme F. Thompson, Between Markets and Hierarchies: The Logic and Limits of Network Forms of Organization (2003).
of norms and mechanisms of monitoring and behavioural modification rather than a binary distinction between law and non-law.

Amongst the most strongly institutionalized inter-governmental networks is the Organization for Economic Cooperation and Development (OECD). The OECD has been an important driver for governance reform across a wide range of areas, including fiscal policies, consumer protection, e-commerce and public management. Many of its activities have spilled over to non-member governments through cooperation with other organisations such as APEC. In terms of orthodox constitutional thinking the OECD appears rather unconstrained in its activities. However, it is apparent that the OECD operates much like a club with members pursuing their own interests through its facilities. These mechanisms create a form of accountability to and oversight by the member states.

The EU has followed the OECD example in the shift towards the open method of coordination and, especially in the development and institutionalization of networks of regulators across various domains. The duty of national regulators to exercise legal duties is constrained by participation in such networks which, we might expect, constrain them to operate within one or more sub-sets of the legally possible interpretations open to them. Participation in such networks is likely to shape one’s world view, and successes and failures in the terms of the network members are liable to meet with approval and disapproval. Such networks are not only a source of constraint, but also potentially of innovation and mutual learning. It is possible that in a well-functioning network behavioural change fostered by learning becomes more important than the constraining effects of network participation.

Are the mechanisms of networks and community more generally appropriate alternatives to orthodox constitutionalism? This is a controversial issue. For some it is unthinkable that orthodox constitutionalism might be displaced by legitimate forms of private governance. The decision of the US government effectively to privatize the governance of the internet architecture when it established the Internet Corporation for Assigned Names and Numbers (ICANN) generated howls of protest for the precise reason that it evaded the constitutional protections and norms associated with the assignment of tasks and powers to public regulatory agencies. No doubt similar objections could be made to networks of public regulators such as those that operate in the EU, where coordination through law has been partially displaced. It has been suggested that ICANN demonstrates the limitations on private networked governance in a case where state involvement to set ground rules and to legitimate processes for decision making would have been constructive. This argues for hybrid solutions, where appropriate to the conditions.

6. Conclusions

Meeting the challenges of regulatory governance requires a concept of constitutionalism which embraces non-state actors and mechanisms for governing which go beyond legal rules – a form of ‘constitutionalisation without the state’. Governance is, of course, a complex matter. We might think about alternative governance structures in terms of which are most likely to have beneficial effects and contrast this with ideas about which are best allied to our values, for example of

100 Gunther Teubner, 'Societal Constitutionalism: Alternatives to State-Centred Constitutional Theory' Ibid..
democratic governance or compliance with some version of the rule of law. My own view is that orthodox constitutionalism, while it might once have been the most appropriate way to think about legitimating a governance centred on the nation state, is not capable of legitimating the diffuse governance patterns associated with contemporary regulation. An alternative narrative offered here seeks to match the variety in governance forms with varied forms of institutionalization which link processes and values of hierarchy, competition and community to appropriate governance forms.

How should we evaluate such an extended constitutionalism in its application to diffuse regulatory governance? An important strand of the literature, and particularly that which focuses on governance networks, noted above, displaces a traditional emphasis on effective control and accountability with a perspective which looks for the capacity of governance structures to promote effective learning, not only about appropriate solutions, but also concerning the nature of the problems to be addressed. To be legitimate such reflexive learning processes, whether stimulated by hierarchical, competitive or community processes, or some combination of these, should engage key stakeholders in the outcomes and, through their processes, command widespread support. In some instances the stakeholder community might be quite narrow. In many instances it is likely to be broad. Such a vision provides an elaboration of, or an alternative to, state-centred versions of democratic government in which more diffuse or nodal forms of democratic decision making substitute for more traditional governance processes.

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