

# Fixing Financial Markets: The Role of Accountability Regimes

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Melvin J. Dubnick  
University of New Hampshire  
[mdubnick@dubnick.net](mailto:mdubnick@dubnick.net)

<http://mjdubnick.dubnick.net>

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Melvin J. Dubnick  
University of New Hampshire

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## Prologue

It takes no more than a passing exposure to some news source to know that we are engaged in an economic crisis based on what many believe to be a major failure of both domestic and global financial markets. Nor does anyone reading this paper at the time of its presentation (mid-April, 2010) have to be told of all the various efforts being made by public officials the world over to find some “fix” that will prevent (or at least minimize) a recurrence. The so-called Great Recession of 2008 continues to ripple through the world economy despite recent signs of “recovery,” acting as a continuous reminder that something must be done to deal with the conditions that brought it about. In the United States we are in the midst of a major push to have Congress adopt proposals for reform that have been on the table in some form for nearly two years.

This paper is the second iteration of a work initially developed in response to a colleague’s challenge to apply what we know about accountability to the problem of reforming financial markets (see Dubnick 2010). While the challenger had in mind a more practical response, what emerged is an ongoing effort to reframe and rethink the financial crisis as a problem of governance. This paper is, in effect, version 2.0 of that initial effort.

After a brief consideration of the dynamics of the “blame games” that generate and shape much of the current reform agenda in Washington, London and elsewhere, I argue for an approach that goes beyond mere tinkering with traditional regulatory mechanisms and instead focuses on the need to reform the “governance regimes” of the financial sector. In the process, I make the case for the existence to two interrelated regimes within the domain of governance requiring attention if we are to make headway in the design of relevant and effective reforms. One of those regimes -- the regulatory, which focuses on governance through control -- has received considerable attention from analysts, and I highlight one effort [by Hood, Rothstein and Baldwin (2001), hereafter designated as HRB] at framing the elements of that regime. The other regime -- accountability, which fosters governance through the creation, allocation and management of expectations -- requires more analytic attention, and I offer the foundations for a framework related to that regime that seeks to emulate the logic of the HRB effort. I then articulate some basic “design principles” that need to be kept in mind as we deal with the future of financial market governance.

## Random Fishing in the Accountability Stream

*"It isn't that they can't see the solution. It is that they can't see the problem."--G. K. Chesterton*

Under optimal conditions, developing long-term and appropriate solutions for the current financial crisis requires a thorough assessment of the problems that generated the situation. Given the complexity of domestic and global financial markets, even the most knowledgeable minds of the era find the analytic challenge daunting.<sup>1</sup> In lieu of some consensus or credible paradigmatic framing of the crisis, policymakers have found other means for filling the "problem definition gap".<sup>2</sup> Thus, although one would hope for a more rational approach to designing policies that might prevent any future recurrence of the current problems, we are currently engaged in multiple "blame games" that will invariably influence the shape of government regulation of financial markets for the foreseeable future.

Beyond the well studied dynamics of political blame avoidance,<sup>3</sup> driving the emergence of "blame games" during times of crisis is the pressure on policymakers as they attempt to fill the gap created by ignorance or uncertainty about the problematic situation they are facing.<sup>4</sup> In addition, those assuming the task of designing policy responses contend with a range of ontological choices. At one extreme is the assumption that the universe generates problems (e.g., crises, disasters) randomly -- i.e., "stuff happens" without any explicable explanation and that the best we can do collectively is prepare for those eventualities that seem to have a greater probability of occurring. A second extreme position -- let us call it the "acts of god(s)" perspective -- views the universe as subject to the whims and unfathomable logic of some supernatural beings or forces that cannot be subjected to our powers of understanding. The best we can do under such assumed circumstances is prepare for any eventuality and engage in considerable praying or perhaps some ritual sacrifices.

Modern policy designers (at least those who accept the basic premises of the Enlightenment) assume some position between those two extremes, and ideally that requires a careful analysis of a problematic condition to determine those causal factors which can be addressed by policy actions -- or at minimum those factors that can be addressed by policies designed to ameliorate the consequences or prevent a recurrence (Lerner & Lasswell 1951; Dror 1970, 1971). For students of the policy design process, the

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1 Economists and other analysts were similarly perplexed during the initial stages of the Great Depression. Keynes drew so much attention because his perspective seemed to fill a void created by the failure of extant theories and models (Minsky 1976).

2 On the nature and dynamics of problem definition, see Dery 1984; Hoppe 2002; Rochefort & Cobb 1994.

3 For example, see Hood 2002; Weimer 2006; Ellis 1994; McGraw 1990 and 1991.

4 Studies of the blame game and similar concepts (e.g., hindsight causal analysis, attribution, issue responsibility) include Iyengar 1991; Strange and Leung 1999; Knobloch-Westerwick and Taylor 2008. Also see Kysar and McGarity 2006.

fact that the universe provides few opportunities for applying objective analysis leads to a fallback position relying on the social construction of problematic realities that can be subjected to some policy fix. Even here, however, uncertainty (and thus controversy) rules unless there exists some "theory" or "model" powerful enough to preclude or direct debates over those factors that policies need to address. This is where "blame games" typically enter the picture.

The "games" themselves are part of a cultural phenomenon basic to modern societies fixated on determining and dealing with the causes of our collective ills. At least in the realm of public policy, secularization and "scientism" have for the most part deposed most forms of fatalism and replaced them with a pragmatic belief that public problems can be analyzed and ameliorated, if not actually "fixed."

Put otherwise, the salience of these games reflects an inherent bias in our policy-making process that seeks out some causal factor that can be acted upon. The urge to take collective (policy) action to deal with a public problem reflects the perceived possibility of taking effective action -- and this, in turn, requires some sense of a link between some factor that can be acted upon and the problem. Deborah Stone (1997) provides a simple but insightful view of options offered in her four types of "causal theories" underlying public policies (see Figure 1). Assuming some degree of consensus among policymakers regarding who or what "caused" (i.e., is to blame for) the problem at hand, these "theories" can have considerable influence on the form and content of resulting decisions. Blame games emerge where such a consensus is lacking, the result being a political struggle to define the cause and (eventually) policy choices that reflect the competition among conflicting views.

Consequences:

<b>Actions:</b>	<b>Intended</b>	<b>Unintended</b>
<b>Unguided</b>	<p><b><i>Mechanical cause</i></b>                      intervening agent                      machines                      trained animals                      brainwashed people</p>	<p><b><i>Accidental cause</i></b>                      nature                      weather                      earthquakes                      machines run amok</p>
<b>Purposeful</b>	<p><b><i>Intentional cause</i></b>                      assault                      oppression                      conspiracies that work                      programs that work</p>	<p><b><i>Inadvertent cause</i></b>                      intervening conditions                      unforeseen side effects                      neglect                      carelessness                      omission</p>

Figure 1: Stone's Types of Causal Theories  
(Stone 1997, p. 285)

In the current debate over the financial meltdown, these "games" have taken a variety of forms -- from well thought out studies to blogger rants to Oxford-style debates -- and not surprisingly are leading to the conclusion that both everyone and no one has some causal responsibility to bear. Was it Wall Street's fault for taking advantage of newly created instruments and schemes to create a bubble that would eventually burst? Or was it Washington's (or London's or Paris') fault for letting down its regulatory guard allowing the banks to run bullishly through the markets? Perhaps it was the fault of the "Main Street" folks who let themselves be conned into believing that home values will forever rise and there were no risks in taking on the debt obligations of a new mortgage or ever higher credit card balances. A convincing argument can be (and has been) made for placing the blame at the systemic level where the interconnectedness of globalized financial markets made the entire network vulnerable to collapse once a critical link (in this case, most point to the US housing market) weakened.

Whatever one can conclude from these various finger-pointing exercises, the significance of these blame games in shaping the causal theories (that will in turn shape future policy) is substantial. Without a consensus view or coherent framing of what caused the present crisis, we should not be surprised to see the emergence of a "hodge podge" set of proposals that reflect political bargaining and compromise rather than what economists regard as an effective and coherent package of solutions.<sup>5</sup>

That noted, the resulting hodge podge is not without its common thread. Focus on the rhetoric used to rationalize proposals put forth by the White House and others, for example, and clearly solutions proffered by a variety of politicians and experts rely on **actions designed to improve accountability**. The underlying logic is simple and sensible on its face: once we determine (correctly or incorrectly) that someone or some agency or some process is to blame, the steps taken to prevent or mitigate a future recurrence must necessarily include some account-giving mechanisms.

But here, too, the lack of a more developed framing logic proves problematic for designing policy solutions. The issue of which accountability mechanisms are relevant to the current financial crisis remains an open question. What does it mean to demand "greater accountability" of the various actors in the financial services industry? The typical responses to that question generate a plethora of "usual suspects." We want those involved -- whether bankers or regulators or customers -- to assume greater "responsibility" for their actions. At the same time we desire that each be "answerable" to their respective principals -- shareholders for the bankers and the public for the regulators. For bankers and others in the corporate sector of this domain, we require that they live up to the fiduciary "obligations" they assumed when taking on their respective positions. As for the regulators, we assume they will be "responsive" to the concerns and complaints brought before them. And for those bankers or regulators

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<sup>5</sup> By the spring of 2009, the main discussion among economists had moved from the academic journals to editorial op-ed pages, the Internet and comments made on podcasts and mass media business news shows. Despite criticisms of government proposals that emerge from the blame game, many of the same experts have contributed to cacophony that generated many and varied proposals.

or customers who might attempt to circumvent or undermine the mechanisms established for those various purposes, we want them to be “liable” for the consequences of their possible mis/malfeasances.

The argument I offer here is that without some effort to define the problems being addressed in a clear and coherent way, reforming the financial services industry by establishing greater accountability will prove difficult at best. The general rhetoric of reform, however, has not fostered any such clarity. “Make them [more] accountable” is the clarion call from all corners of the policy-making world. And at least to this point in the crisis, that rhetorical theme has trumped any effort to focus attention on exactly what it is we wish to accomplish by declaring our desire for more accountability.

For many students of the public policymaking process, the present situation confirms the relevance and credibility of what is called the “garbage can model” (GCM) of decision-making. Originally articulated as model to explain decision making in “organized anarchies” such as universities,<sup>6</sup> GCM has been transformed into a widely used model of the complex policy-making process in the US which has features resembling anarchical arrangements. Perhaps the best know of these GCMs was developed by John Kingdon (1984; see Mucciaroni 1982) who described the process as involving three independent “streams”: a “problem” stream, representing the current flow of issues of potential interest to policymakers; a “policy” stream of possible solutions, many seeking a problem to deal with; and a “political” stream of various actors whose interests and activities vary over time. For Kingdon and others who use this model, the adoption of a policy involves a fortuitous convergence of these three streams during a “window of opportunity” when all three happen to flow together.

Applied within a particular “policy domain” such as the reform of financial markets, this multiple streams model helps make sense of the current situation where the ongoing blame game generates multiple problems (related to a range of accountability deficiencies) to be “solved”, with policymakers responding by throwing various accountability-based solutions at those situations that seem to be the most salient at a given moment.

Perhaps the most obvious example was the flare up involving the infamous “retention bonuses” at AIG. In the midst of a major effort to design a reasonable and feasible plan for relieving banks of their “toxic assets” (which was itself filled with many different accountability-related challenges), the primary policy actors had to contend with a media-fed public outrage by attempting to hold AIG “to account” for what many perceived as a violation of the public trust and treasure. Executive compensation restrictions had, in fact, been part of the ongoing deliberation of how to design the TARP program from the outset, but the issue was plucked from a problem stream filled with many more (and less) significant issues, and the resulting “crisis” generated a frenzied search for an quick-fix response from among those found in the

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<sup>6</sup> For the original version of the model, see Cohen, March and Olsen 1972; also March and Olsen 1976 and Cohen and March 1986,

stream of policy instruments that would satisfy the whirlwind that brought turbulence to the political stream (Webel 2009; Thatcher 2009).

The AIG episode turned out to be the first of many similar flash points that have emerged intermittently as various “rescued” banks publicized their compensation plans. But with this and other issues, there is nothing in the public record to indicate that a more reasoned (non-GCM-like) process is being applied in response. Faced with specific issues related to a particular aspect of the financial crisis, policymakers will respond with accountability mechanisms pulled from the policy stream that seems the best fit to deal with the narrowly defined problem.

Put another way, the ambiguous nature of the rhetorical calls for “greater accountability” are producing the expected response (at least under the GCM): an ad hoc proliferation of policy proposals that are incoherent and inconsistent at best. In some instances we have reforms designed (intentionally or not) to strengthen oversight and control -- of both the regulated and the regulators! At the same time, demands for greater “transparency” and open deliberations are made of all parties. In other cases we find accountability mechanisms aimed at assuring that the internal decision processes (again, of both the regulated banking community and the regulators) follow a certain pattern and that the targeted decision makers behave in an “ethical” or appropriate way. Still other responses impose “high stakes” performance standards and measures designed to direct and “motivate” the various agents and agencies involved.

Each of these policy responses make sense considering the narrow and specific nature of the problems drawn from the stream at a given time. The more general question is whether, when taken together and assessed in their entirety, they can constitute an effective effort to deal with the need for “greater accountability” in the financial services domain.

## **Framing the Design Problem**

If we are to develop solutions to the current financial crisis, we need to begin by articulating and (re)framing the problem, and here we can start with a basic assumption about the corporatized market that has been accepted by both political scientists and economists since at least the 1930s: the central problems are those of creating and sustaining “good governance”.<sup>7</sup>

As with all terms that are part of the common parlance of political dialogue (e.g., power, sovereignty, etc.), reference to the concept of governance requires some analytic clarity. Among those engaged in

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<sup>7</sup> The use of the phrase “good governance” may be troublesome for some, not merely for its obvious normative implications, but also due to its association with “neo-liberal” policies of the World Bank and International Monetary Fund. For example, see Finkelstein 1995 de Alcántara 1998, Weiss 2000, Doornbos 2001, Aguilera and Cuervo-Cazurra 2004, and Bourdieu 2005, pp. 10-12. In the analytic exercise that follows I attempt to circumvent both the normative and ideological implications of the concept.

the analysis of government, however, the focus of attention is so wide ranging that any study must assume an arbitrary position regarding the concept. Thus, for many analysts governance is “what governments do” -- the tasks and functions they carry out as the legitimate controllers of the machinery of the modern state (e.g., Rose 1976). At the other extreme are those who regard governance as “socio-cybernetic systems” and “self-organising networks” which emerge as authoritative sources of control within and among all forms of organised life -- from the family unit to the modern state and global networks (Rhodes 1996; Stoker 1998). Taking a somewhat middle course are analysts such as Oliver E. Williamson (1994, 1998) who traces the study of governance to the work of John Commons (1932) and Ronald Coase (1937), and defines it as the examination "of good order and workable arrangements."

For present purposes we will follow that “middle road” definition and assume that the focus of our policy design task is to articulate reforms that can be made to enhance the “good order and workable arrangements” that “govern” the form and operations of today’s financial markets.

Another central tool for this design task is that of “regimes,” a concept often used by students of governance whether they are focusing on states, networks or formal organisations. In conventional discussions about politics, the term "regime" is loosely applied to types of political systems or styles of governance (e.g., democratic regimes, authoritarian regimes, Stalinist regimes) or the government of a country that has been ruled by some person or party for an extended period (e.g., the Castro regime, the Communist regime).<sup>8</sup>

Among scholars who study governance, the term "regime" is typically assigned to those politically relevant social and economic arrangements that endure overtime to form the setting within which governments (and political systems in general) operate. More specificity, what the term "regime" means analytically depends on the scope, breadth and depth of the domain of governance action to which it is being applied. For some, regimes constitute the basic moral order or (in Charles Taylor's phrase) social imaginary (2004) that influences the form, direction and force of governance. In Taylor's sweeping historical analysis and critique of the modern "secular" age (2007), for example, the term regime is synonymous with the underlying "moral order" of a society, and he regards changes and shift in regimes (i.e., social imaginaries) to be rare and revolutionary.

For others, regimes are reflected in the patterns of governance that emerge within settings where the traditional structures and mechanisms of government are not available. Students of world politics have paid growing attention to the role that both formal and informal international regimes have played (and

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<sup>8</sup> There is notably a negative, judgmental sense implied in the popular use of the word "regime" evidenced by the fact that the concept is rarely applied to US regimes (typically labelled "administrations") or many parliamentary regimes (which are noted as "governments" in the media).

continue to play) in transnational relationships and the development of the global economy.<sup>9</sup> Another group of scholars, many associated with the public choice perspective that spans economics and political science, regard a regime as the "logic" of governance (e.g., Madisonian, Weberian) that develops within a constitutional ordering of political and social relationships (see E Ostrom 1990; Schlager & Ostrom 1992; see also V. Ostrom 1974). At an even more specific level, students of regulatory policy apply the term regimes to the range of strategic approaches used within a particular policy arena (e.g., utility pricing, telecommunications, etc.) (Schmalensee 1989; Weisman 1993; Rust & Rothwell 1995).

For present purposes, the concept of regime will be applied to two governance arrangements that are most salient in the reform of the financial services sector. A *regulatory regime* involves arrangements of institutions, norms, values and relationships intended primarily to exercise some *degree of control* over the governed acts and actors. It is somewhat synonymous with Jessop's "regulation approach" view of capitalist economies, involving "economic and extra-economic institutions and practices which help to secure, if only temporarily and always in specific economic spaces, a certain stability and predictability in accumulation -- despite fundamental contradictions and conflicts generated by the very dynamic of capital itself" (Jessop 1997, pp. 287-288). Regulatory regimes can take explicit form as manifested in legal and bureaucratic frameworks<sup>10</sup> that generate and enforce laws and rules; or they can take more implicit form in the development of a Foucauldian "governmentality" that (in its most extreme) fosters a sense of panoptic oversight and monitoring (Rose & Miller 1992; Rose 1999, 2000).

Among the most useful, design-relevant explications of regulatory regimes is that offered by Hood, Rothstein and Baldwin (HRB) in their watershed The Government of Risk (2001). Although directly addressing social risk policies in the United Kingdom, their study and its comprehensive framework has a broader applicability through its focus on the variations of means and mechanisms used to control individual and collective risk behaviour across several different policy domains, including those related to domestic and global marketplaces. Central to the HRB construct (see Figure 2) are three core forms of "control-components" used to deal with risk within an examine domain: information gathering, standard setting and behaviour modification. These are then explicated in terms of the context (type of risk, public attitudes, organised interests) and content (size, structure and style of regulatory effort). The result is an analytic frame developed to describe (for heuristic purposes) and empirically examine (for research and theory development/testing purposes) (Hood & Rothstein 2001) regulatory regimes aimed at risk. In addition, the dimensions used in the framework can be articulated in forms that facilitate at least comparative (if not even more systematic) assessment. As significant, those interested in generating solutions to problems plaguing a particular policy domain can certainly find value in the design elements implied in the HRB analytic scheme (Levi-Flaur 2006).

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9 This work has found explicit expression in the work of Oran Young (1980, 1982, 1986, 1999); Stephen Krasner (1982, 1982a); and John Ruggie 1982, 2006..

10 The "regulatory state" concept that reflects this view is found in Majone 1997, 1999, 1999a; also see Moran 2001.

Within the governance setting there is a second and quite necessary complement to the regulatory regime that fosters a sense of responsibility and obligation among actors in the domain. This **accountability regime** involves arrangements and “assemblages” (Sassen 2008, p. 61) of institutions, norms values and relationships related to the fact that governance involves more than a web of control components and associated mechanisms; governance is based as much on some normative order -- a “moral community” context or “accountability space” within which the governed population (of acts and actors) necessarily operates. It is within that normative regime space that standards of appropriate and ethical behaviour -- in very general term, **expectations of responsible behavior** -- are established and sustained, and where trust can be nurtured.

<b>Control components:</b>			
	<b>Information gathering</b>	<b>Standard setting</b>	<b>Behaviour modification</b>
<b>Context:</b> e.g., type and level of risk being tackled, nature of public media attitudes, configuration of lobbies and organized interests	Example: risks individuals can assess at low cost vs risks assessable only by professionals or at high cost	Example: risks involving high stakes for organized groups vs risks with no lobby groups	Example: risks where mass public opinion resist state control vs regulation ‘with the grain’
<b>Content:</b> e.g., regulatory stance, organizational structure, operating conventions and regulator attitudes	Example: active vs passive information-seeking by regulators	Example: cost-benefit vs technical feasibility approaches to goal setting	Example: price signals vs command approaches to control

Figure 2: HRB’s Control Components and Regulatory Regime Content and Context

Seen from a domain perspective, governance primarily (but not exclusively)<sup>11</sup> involves **both the control of risk and the management of expectations**. A governance effort involves both, and an effective (“good”) governance effort (which is the assumed goal of policy reform) is one that treats the regimes that address these two functions as complementary.

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<sup>11</sup> Governance, of course, serves many other purposes. For example, see Rose 1973, 1978; Peters 1996; Peters & Pierre 1998.

Applying this two-regime perspective to the current efforts to reform the financial services market, it can be argued that most current reform efforts have been focused on the regulatory aspects of the general governance problem. In part this contention reflects the “blame game” approach that has dominated explanations of what went wrong in the financial sector; in the aftermath of a crisis, when all or most systems have failed or seem in disarray, the regulatory mechanisms (and regulators) provide easy targets for blame gamers. In addition, the concentration on regulatory regime reforms reflects the fact that (re)designing control regimes seems less challenging than designing accountability regimes.

A more fundamental view of the problem is conceptual. The difficulty with designing reforms for the accountability regimes of governance is traceable to our inability to understand and appreciate what this important area of governance entails. In the remainder of this paper, I explore the nature of the accountability regime with the intent of constructing a preliminary framework for the design of reform policies that can offer a more effective approach to solving the governance issues that plague that arena. While the goal is to develop an analytic frame of equal utility and power as the HRB scheme, what follows should be regarded as preliminary at best.

## **Mechanisms and Moral Standards**

Despite the drawbacks of following conventional blame gaming approaches to determining the problems of a policy domain in crisis, there are some insights to be gained by examining the resulting political rhetoric and policy responses -- especially their common focus on the need for “greater accountability.”

In the general “talk” about reform, accountability emerges in two very different but interrelated conversations. In one conversation, accountability (or the lack thereof) is being discussed as a key factor in bringing about the “meltdown” of economic relationships built around the high-flying financial services industry. Accountability, in some form or another, is viewed by the participants as a problem -- perhaps THE problem -- that needs addressing.

The other conversation (occurring almost simultaneously) is focused on solutions rather than problems. The major refrain here -- repeated constantly in more rhetorical settings -- is the need for “greater” and “more” accountability as a (if not THE) solution to that very same crisis.

This simple observation about the role of accountability as both problem and solution -- cause and cure - - begs for clarification if we are to make some sense of the accountability regime’s place and role in governance. What does accountability mean to those engaged in these searches for causes and cures, and in what way(s) do various views of accountability impact on our understanding of the financial crisis and/or our responses to it?

Interestingly, the myopic obsession with *regulatory* control comes into play at this juncture. In discussions dealing with the search for causes of the crisis (i.e., the “blame game”), the failure of

accountability is typically (if not always) articulated in terms of some specific institutional mechanism or policy instrument failure. The list of suspected culprits ranges from the insufficiency of basic managerial controls and internal corporate governance mechanisms, to the lack of transparency and due diligence, to lax enforcement of banking and securities regulations and the absence of effective oversight of regulators by executive, legislative or judicial officials. Shortcomings abound in all these assessments of the problems -- shortcomings in the sense that the regulator or regulated party is *just not living up to expectations*. Regulatory regime control components overlap with -- perhaps are actually embedded in (Granovetter 1985, 1992; also Bourdieu 2005) -- the accountability regime. Each and all are regarded as part of an accountability infrastructure composed of various tools (e.g., oversight, audits, inspections, investigations, chains of command, etc.) that share a defining characteristic that distinguished them from other control components: each operates by establishing account-giving relationships among at least two parties in an organized effort that **addresses the need to deal with unaddressed or unfulfilled expectations**.<sup>12</sup>

Viewed narrowly as account-giving mechanisms or instruments, accountability is a means for the management of expectations and takes on the characteristics of a technical feature of the financial marketplace, a functional (often institutionalized) part of the economic, political and social relationships that comprise this sector. It follows that when the focus turns to failures of accountability (i.e., these “mechanisms”) as the cause of the current crisis, attention necessarily turns to the absence or breakdown of social relationships and expectations. The “cure” implied in that analysis most often finds expression in proposals to repair or replace the failed or damaged mechanisms.

But such mechanisms must be regarded as only part of the accountability regime construct. An alternative dimension of accountability is also at work in the cause/cure discussions, one that regards accountability as playing more of a normative role than a technical one. Here the talk is not about the failure of mechanisms or instruments of account-giving, but rather **the failure of more amorphous**

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<sup>12</sup> The idea of an “account-giving relationship” demands some clarification at this juncture in regard to four points. The first is to highlight that we are dealing with social relationships, and therefore these have to be understood as fundamentally *social* mechanisms despite the fact that we often perceive them too narrowly in strictly formal or legalistic terms.

Second, although frequently associated with the logic of principal-agent relations (especially when operationalized in academic models), such relationships do not necessarily involve hierarchical or super/sub-ordinate arrangements. At least in theory (and more often than is often acknowledged, in practice), account-giving relations can be horizontal as well as vertical, bottom-up as well as top-down -- and even circular in form (e.g., the “reflective” practitioner).

Third, these relationships are based as much (if not more) on expectations as they are in actions. Often it is the anticipation of claims on one’s account-giving capacity that determines the effectiveness of an accountability mechanism. Anxiety about who might seek an account, what action one might be held to account for, and when one might be called to account -- all play major roles in shaping the relevant relationships. For more on this point, see Darwall 2006).

Finally, these account-giving relationships cannot be viewed in isolation from other social relations, including other account-giving claims. The existence of multiple, diverse and potentially conflicting expectations is itself to be expected in the world of accountability mechanisms.

**conditions that foster expectations management** such as a moral sense of responsibility, fiduciary obligations, responsiveness, liability, etc. These reflect the idea of accountability as providing the moral, normative setting for the operations of financial markets. The emphasis here is on the premise that any set of social relationships -- especially those involving complex interactions and transaction such as found in global financial markets -- **requires some commitment to a functional and effective set of expectations in the form of rules, norms, mores**. Among those conversing from this perspective, it is the absence or ineffectiveness or collapse of these normative (i.e., "moral") standards that is at the heart of the current crisis. The implied "cure" would be whatever policies which might restore or reconstruct that normative infrastructure (*cf*, Lane 1997; also May 2005, 2007).

Figure 3 attempts to summarize the implications of this distinction (simplified as accountability-as-[control] mechanism and accountability-as-[normative] setting) for the discussions about causes and cures of the present crisis.

		<b>Focus on:</b>	
<b>Perspective:</b>	<i>Cause</i>	<i>Cure</i>	
<b>Accountability-as-Mechanism (i.e., control)</b>	<b>Failure of instrument</b>	<b>Reform, replace, repair the instrument</b>	
<b>Accountability-as-Setting (i.e., normative infrastructure of expectations)</b>	<b>Absence or collapse of norms, mores, standards</b>	<b>Reestablishing, rebuilding moral community based on effective norms/standards</b>	

Figure 3: Accountability as Cause/Cure

The implications of this framework for designing policy responses to the financial crisis will be discussed in the next section, but there are two additional observations that require attention before moving to that point.

First is the extent to which one of the perspectives dominates the most important of the conversations about the financial crisis. Where those conversations really "matter" -- in those venues where

policymakers talk about “causes and cures” -- the mechanism perspective drowns out the normative infrastructure (setting) view. In this and other areas where the issue is the breakdown of an ongoing system, “technical” explanations usually hold sway, and not necessarily because they are more credible or convincing. Rather, as complements to the regulatory control regime, they tend to be “easier” to grasp conceptually and have the benefit of generating relatively quick solutions. If the problem is determined to be lax enforcement of banking regulations, then enhance the enforcement power of regulators and back it with more funding. If the “problem” is lack of transparency in the operations of hedge funds or private equity firms, then require more reporting and openness. In both examples, there is a clear sense that regulatory control will be enhanced, but only a vague hope for the more responsible behavior on the part of the regulated parties. Nevertheless, such reforms are proffered as having enhanced accountability. Whether they actually do so (i.e., fostered more responsible behavior) is an empirical question.

Which leads to a second point, namely the ironic tendency of policymakers to rely on the rhetoric of accountability in their rhetorical rationalizations for mechanism-focused policy decisions. The justification for undertaking regulatory-based reforms is to create a “more responsible” market or to make certain actors “answerable” and “liable” for their actions. There is an assumed effective link between the exercise of control and the enhancement of responsible behavior -- a linkage that has rarely been tested in the governance context let alone empirically proved. Each of these rhetorical flourishes at minimum implies the existence of that connection and begs the question about the need for some moral community that provides a normative understanding of what constitutes (ir)responsible and (in)appropriate behavior.

To summarize briefly, when it comes to accountability regime issues raised by the current financial crisis, (1) there are at least two conversations taking place, one focused on the role of accountability (or lack thereof) in creating the crisis (the “cause” conversation) and the other positing accountability as a major part of the solution (the “cure” conversation); (2) beneath the surface of these conversations are two very different perspectives on accountability, one perspective viewing it as social mechanisms and policy instruments rooted in “account-giving” relationships (accountability-as-mechanism) and the other seeing accountability as providing the moral setting for the market (accountability-as-normative infrastructure); (3) among policymakers (the conversations that really matter), the mechanism view prevails as they seek to match control-based technical solutions to technical problems perceived as regulatory; (4) but the rhetoric of accountability-based reform remains normative-based and is tied to sense that what is needed is more responsible, responsive, answerable, etc. behavior among market actors.

Underlying the present effort is the belief that there is a more substantial case to be made for taking accountability-as-setting (normative infrastructure) view seriously, not only as part of a more general theory of policy domain governance, but also as the basis for policies that can have a real impact on the future operations of global and national financial markets. But to put that belief to work requires that we develop an HRB-like analytic frame that can do more than help us appreciate the importance of the

accountability regime as part of governance. We need a “framing” that allows us to focus on those elements that comprise the accountability setting in order to facilitate efforts to describe the regime, assess its effectiveness and (where possible) assist in the design of solutions to the broader governance problems.

## **Articulating Design Options**

An effort to emulate the HRB framework for accountability regimes runs into an immediate problem, for the core components of accountability (as imagined here) encompasses normative settings as well as “mechanisms”. While contextual factors play a role in the HRB scheme, they do so as independent or intervening variables impacting the form and content of the core control-components. But, as noted below, in accountability arrangements many aspects of the setting are themselves core components of the regime.

Beyond including those “setting” factors as core components, our framing should be meet two additional, interrelated criteria. First, it should be empirically inclusive and capable of encompassing the range of actionable options that are proposed to deal with the problematic conditions “greater accountability” is intended to address. Second, the options it includes should be problem relevant and expressly aimed at dealing with the causes and/or conditions of the problematic situation. Excluded under this framing scheme would be pseudo-proposals that amount to mere symbolic expressions of the need for reforms and those designed to solve problems outside the scope of policy problem. While symbolic gestures such as a rhetorical call for making the financial system more accountable may serve important political purposes (e.g., for the mobilization or acquiescence of publics)(Edelman 1964, 1971), they would fall outside our frame unless accompanied by some articulated agenda for reform. Similarly, options aimed at more fundamental changes (e.g., changing human nature or radically altering the general economic system) would be outside the scope of the framing given is “practical” focus.

There have been at least three explicit efforts to frame accountability regimes, the first related to reforms that reshape the context and conduct of accounting, auditing and other financial management operations;<sup>13</sup> a second involved the development of an “accountability model” developed by Fisse & Braithwaite (1988, 1993) to deal with corporate crime; and a third examining the increasingly complex arena of nonprofits operating in a global context.<sup>14</sup> Almost all treat accountability as a variant of regulation and control, and not surprisingly are preoccupied with viewing it in “mechanism” terms. As such, they fail to stress the distinction between the different role that such mechanisms play in regimes

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13 The major work in this area is attributable to James Guthrie and his colleagues at the University of Sydney. See English & Guthrie 1991; Guthrie 1992, 1993; Parker & Guthrie 1993. Also see Broadbent & Guthrie 1992.

14 See the work of Alnoor Ebrahim and his colleagues: Ebrahim 2003, 2003a, 2006, 2009; Ebrahim & Heerz 2008; Ebrahim & Weisband 2007 (esp. Weisband & Ebrahim 2007).. Also see Jordan & Tuijl 2006.

of control and regime of managed expectations (i.e., responsibility). The task here is to construct a framework that stresses that distinction (*cf* Mashaw 2006).

Turning specifically to the core components of the accountability regime, the range of options for “greater accountability” reforms can be usefully framed by focusing on two common features of most proposals: (1) the extent to which they seek to specify the activity and actions (i.e., expectations) of those being held accountable and (2) the degree to which the accountable agent is given some degree of discretion to act (i.e., autonomy) on those expectations.

		Specificity of accountable activity (i.e., expectations)	
		Low	High
Autonomy of accountable agent	High	<p><b>Constitutive Accountability</b> Creation of “accountable space” for development and operation of internalized norms and standards (i.e. expectations)</p>	<p><b>Managerial Accountability</b> Set “what” agent is accountable for (objective or standard), allow agent to determine “how” to meet expectations</p>
	Low	<p><b>Regulative Accountability</b> Creation/externalized oversight of (expected) actions of agent within “accountable space”</p>	<p><b>Performative Accountability</b> Set “what” agent is accountable for and “how” to proceed to meet those expectations</p>

Figure 4: Accountability regime’s core component types

Of the four resulting core component types, the **performative accountability** reforms are most closely associated with the accountability-as-mechanism perspective. Here the assumption is that greater accountability requires the specification of certain (expected) actions and behaviors which are to be mandated and enforced, typically by a governing authority outside the organization (*cf* Fisse & Braithwaite 1993). These reforms stress the control functions of accountability, and they are not uncommon in the banking industry. They are so pervasive, in fact, that many view them as the very definition of accountability. Nevertheless, what differentiates these account-giving performatives from controls is the underlying intent that the performance (conducting an audit, publishing the results, etc.) will lead to responsible behavior. Here there is an implied link between required behavior and the sense of responsibility which it is assume to generate or awaken in the target population. The strength of this assumed link is very high, and therefore clearly stated and strictly enforced reporting requirements by a

variety of regulatory and other oversight agencies regarded as part of the necessary infrastructure for conducting business in many of the world's jurisdictions (Ball 2001).

Reforms based on the logic of **managerial accountability** differ from the performative in allowing greater discretion to the accountable agent while at the same time holding it accountable to meeting a specified objective or standard. Reflecting the growing cultural acceptance of managerialism,<sup>15</sup> it is based on the assumption<sup>16</sup> that those "professionals" who operate regulated organizations are by definition (after all, they are professionals) predisposed to responsible behavior once provided with guidance regarding the ends to be achieved. A law or regulatory body might require, for example, that a bank chartered to operate within a state or community commit at least x percentage of its loan portfolio to local businesses or individuals. The standard for conducting business is set, but how they go about do so is left to the bank and its management. This form of accountability assumes that those professionals who manage the financial institution will act, as Berle argued in 1932, "more as princes and ministers than as promoters or merchants."<sup>17</sup>

While the mechanism perspective characterizes both performative and managerial accountability approaches, the regulative and constitutive forms rely more on what can be termed an "accountable space" perspective. Here accountability is viewed as a more general context or setting -- what Bourdieu terms a "field" (Bourdieu 1989; Boudieu & Wacquant 1992) -- within which relationships occur rather than as itself a specific relationship per se. These accountable spaces can be characterized by both their structure and substance.

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15 Berle and Means (1932) first described the logic of this approach in the corporate world when they presented their classic exposition of the transformation of the modern corporation into a professionally managed organization. "A management may well insist on as free a managerial hand as possible as to how it shall run its business," they observed. "Nor has anyone grudged managements this group of powers, not only in law but in ideology. No better principle in carrying on business has yet been worked out than to find able men and give them the completest latitude possible in handling the enterprise" (p. 60). Also see Mason 1958; Preston & Post 1974; Miller & O'Leary 1989.

16 Although this assumption originated in the private sector, it has been most often critically examined with public sector contexts. On the history of private sector managerialism, the classics are Burnham 1960 and Chandler 1977. The classic expression of a positive view of public sector managerialism was found in Friedrich 1940. The recent New Public Management reforms that took root in New Zealand, Australia, the UK and Canada had a strong managerial accountability component; see Pollitt 1993; Pollitt & Bouckaert 2000; Cochrane 1993; Campbell; and Hood 2001).

17 Berle 1932, pp. 1366-1367. In the same publication (p. 1377) he offers the following: "Most students of corporation finance dream of a time when corporate administration will be held to a high degree of required responsibility -- a responsibility conceived not merely in terms of stockholders' rights, but in terms of economic government satisfying the respective needs of investors, workers, customers, and the aggregated community. Indications, indeed, are not wanting that without such readjustment the corporate system will involve itself in successive cataclysms perhaps leading to its ultimate downfall."

Structurally, they exist as arrangements within parameters set by a range of normative constraints in the form of general roles and rules that shape the expected relationships that take place within that space (*cf* Fligstein 2001, Preda 2009, and Davis 2009.). **Constitutive accountability** reforms<sup>18</sup> focus on the establishment and adjustment of those parameters, effectively constituting (or reconstituting, as the case may be) the environment within which accountable behavior occurs. Again, we find these types of reforms to be familiar in the financial markets. The roles and rules required by accountability “regimes” for financial institutions varies depending on the “constitutional setting” within which they operate. With both deregulation and liberalization of banking laws over the past several decades, the number of such settings has multiplied. This has created opportunities for banks to “shop around” for what they regard as more suitable accountability regimes both domestically and globally.

**Regulative accountability** comes into play when the substance of those roles and rules require the active monitoring and oversight of an accountable agent by a regulatory overseer. The logic of this form of accountability is drawn from the regulatory regime, but the design premise is different. The assumption here is that the target population will be more “responsible” in exercising discretionary behavior (i.e., meeting normative expectations) knowing that there is a regulatory agent overseeing what is taking place in the accountability space. Parker uses the term “responsive regulation” to capture this approach: “Simple deterrence will often fail to produce compliance commitment,” she argues, “because it does not directly address business perceptions of the morality of regulated behavior -- it merely puts a price on noncompliance, and the ability of that price to deter misconduct will depend on the operation of the deterrence trap. Responsive regulation, by contrast, seeks to build moral commitment to compliance with the law” (Parker 2006, p. 592; also see Ayres & Braithwaite 1992). For example, the proposal to establish a consumer protection agency with jurisdiction over credit products is in part designed to enforce “control” provisions of the law. But the agency is intended as well to monitor complaints about credit providers from consumers and even rate card services, thereby giving the financial institutions reason consider a more responsible (“customer friendly) approach to doing business.

As the core components of accountability regimes, each of these stresses the need to establish and foster responsibility (i.e., expectations management) over the demand for control. Even the form that comes the closest to a control mechanism -- performative accountability -- differs in purpose (if not in content) from the behavior modification mechanisms represented in the HRB frame. Consider, for example, the requirement in Section 302 of the 2002 Sarbanes-Oxley Act<sup>19</sup> that corporate CEOs and CFOs attach their signatures to mandated audit reports that essentially certifies the “appropriateness of

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18 Perhaps the most relevant and useful approaches for analyzing these types of reform is found in the work of Elinor Ostrom and her colleagues whose research has focused on solutions to common pool resource problem. See Ostrom 1990, 2005; Dietz, Ostrom & Stern 2003.

19 For an examination of the role of accountability in provisions of Sarbanes-Oxley, see Dubnick 2007.

the financial statements and disclosures contained in the periodic report, and that those financial statements and disclosures fairly present, in all material respects, the operations and financial condition of the issuer.” Contrast that requirement with a provision in Section 401 that specifies the “annual and quarterly financial report . . . shall disclose all material off-balance sheet transactions” and “other relationships” with entities that can materially have an impact on the financial condition of the issuer. The latter is an explicit instruction seeking a behavioral change, while the former is at best an indirect attempt to foster a more responsible approach to the way corporate executives do their jobs.

Of course, that type of distinction is often blurred by the fact that the two regimes overlap in the overall scheme of governance. Recently imposed provisions to control compensation received by executives in banks that received “bailout” funding from the US TARP program can be regarded as driven by both regulatory and accountability regime drivers. The regulatory aspects stress a combination of both standard setting and behavior modification by the subject firms, but implied in the action is the message that those executives who are assumed to have played a role in the policy-precipitating crisis need to learn their lesson and act more responsibly in the future.<sup>20</sup>

With the core conceptual components of the accountability regime established, and continuing in the attempt to emulate the HRB approach, we now turn to those factors that lead to variations in accountability regimes across and within policy domains. As reflected in Figure 5, there are three likely sources that determine such variation: content, context, and conditions.

Regarding content, as conceptualized here accountability regimes are primarily about the creation, allocation and management of expectations, thus making variations of expectations extremely important in the description, assessment and design (and reform) of domain governance. Approaching expectations analytically is no simple task (e.g., Dubnick & Romzek 1993) given its sometimes implicit nature. For example, while it might be possible to articulate some legal requirements and general standards of behavior that we expect from domain actors (e.g., that they perform their tasks with “due diligence”), there is also a more general, often unarticulated sense of “responsible” and “appropriate” behavior that plays an important role in accountability regimes.<sup>21</sup> For present purposes, those more amorphous standards can be shifted to the “context” factor category, leaving “content” to reflect expectations that have an explicit presence in the regime.

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20 See Fisse & Braithwaite 1993. There is a sense of collective indignation and retribution also associated with those efforts.

21 The “logic of appropriateness” factor in choice is likely to play a significant role in the further development of this scheme; see March & Olsen 1995; 2004.

<b>Types of accountability</b>				
	<b>Performative</b>	<b>Managerial</b>	<b>Regulative</b>	<b>Constitutive</b>
<b>Content</b> e.g., actions that assert, clarify or remind actors of what is normatively expected or appropriate	Meaningful narratives; required symbolic gestures; mandated rituals, e.g. quarterly reports	Mission, goals, direction; e.g., granting of limited discretionary authority	Rules, standards, oversight, sanctions; e.g., fiduciary responsibility	Institutional parameters, norms; e.g., assumed due diligence
<b>Context</b> e.g., setting or medium for carrying out expected actions	Publicity, media	Organizational	Laws, oversight	Markets, assumed integrity of actors
<b>Conditions</b> e.g., circumstances, triggering situation or event	e.g., scandal, poor reputation, misfeasance, malfeasance (Sarbanes-Oxley provisions)	e.g., low or poor performance, productivity, etc. Ineffectiveness	e.g., misfeasance, malfeasance; noncompliance (SEC suit against Goldman Sachs)	e.g., market failure, government failure (threat of major market reform; threats from political movements)

Figure 5: Framing the Accountability Regime

Having put aside the unarticulated expectations, getting a useful analytic handle on the expectations content of accountability regimes is still quite challenging. Expectations can vary from very specific requirements, often laid out in laws and regulations, to those such as due diligence and fiduciary that involved very general standards (with real consequences for actions) applied from case to case. Beyond their specificity, other dimensions of expectations that come into consideration include (in no particular order):

- the *scope* of their coverage: for example, does the expectation for transparency apply to all behavior within the domain, or are their some are (e.g., proprietary information) that is exempted?

- the *distribution* of expectations within the domain: does it apply to the entire population of targeted actors in a domain (e.g., all commercial banks) or only to those that are “too big to fail”?
- the *salience* of a given expectation or set of expectations within the domain: just how important is the standard among the range of expectations applied in the domain?
- the *stability* of the expectation over time: is the standard expressed in an expectation going to endure overtime, or does it shift from circumstance to circumstance -- and, if so, is their a pattern to that “shifting”?
- the *source(s)* of the expectation or standard: does it emerge from within the domain or is it imposed from outside, etc?
- the *purpose* or intended function of the expectation: is it regarded as a means for promoting integrity and trust among domain actors, or is it focused on enhancing the efficiency or fairness of domain actor actions?

While not exhaustive, this list of content factors indicates how complicated accountability regimes can be -- and how challenging the design task is likely to be as well. The situation is further complicated by the fact that context matters as much as content when it comes to accountability. For present purposes, we will differentiate between the more general (i.e., background) context from the immediate circumstances having an impact on the operations of the regime (see discussion of “conditions” that follows).

There are a number of relevant analytic approaches to the general context of accountability regimes that can be applied for this framing project. The “group-grid matrix” typology developed initially by Mary Douglas and Aaron Wildavsky<sup>22</sup> highlights the variation in expectations that emerge from five cultural orientations that emerge from differences along two dimensions: the extent to which one perceives the world from a vantage point that stresses collective (high group) or individual (low group) approach to problems, and the extent to which one regards oneself as constrained (high grid) or allowed discretion to act (low grid) by the demands of society. The four major types of actors that emerge from this framework relate to expectations differently, ranging from the egalitarian whose expectations are shaped by a strong identity with group values and a high sense of efficacy to the fatalist whose expectations are neither coherently organized nor actively pursued. Between the two extremes are the cultures of the market (individualist) and the organization (hierarchist).

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<sup>22</sup> See Douglas & Wildavsky 1982; Wildavsky 1987, 1988, 1989; Douglas 1992, 1999; Thomson, Ellis & Wildavsky 1990; Ellis & Thompson 1997. Also see Hood 1998. For an overview, see Mamadouh 1999.

Alternatively, Pierre Bourdieu's view of social contexts as "fields" of often competing "forces" can provide significant insights into the factors that shape expectations and shape/drive the accountability regime. In his examination of economic markets, for example, he attributes the decisions of various actors to their "positions" within the fields as well as their "dispositions" (which he often terms "tastes", but which can be treated as expectations) related to the choices and options before them (Bourdieu 1977, 1985, 1898, 1990, 2005).

Which of these (or other)<sup>23</sup> models of context variations can prove most useful within this regime framework awaits further exploration. In Figure 5 some relevant contexts for financial markets are offered for each of the accountability regime type, and at this point these are merely analytically speculative. What needs to be emphasized is that any framework for designing financial market reforms must take into account the variability of accountability regimes across different contexts and cultures broadly defined.

The same holds true for "conditional" factors -- the more immediate political, economic and social circumstances -- in which reforms would be implemented. The HRB framing of regulatory regime context is relevant here. Among the factors they highlight are three major sources of "pressure" at work within risk regulation regimes: market-failure pressures that generate demands for preemptive or corrective policies; opinion-response pressures emanating from the general public; and interest-driven pressures that reflect stakeholder demands (HRB, pp. 61-67). In addition, the current forms and styles of policymaking styles in different countries are an essential set of factors that require attention (Löfstedt et al 2001). Many of the "conditionals" reflect noted as examples in Figure 5 are drawn from the blame game rhetoric of the current financial crisis, and in essence can be categorized and analytically approached using the HRB framing.

Of course, what is provided here is merely a preliminary framing of the that requires further elaboration and application to current accountability regimes. Only through enhancing our capacity to describe the elements of accountability regime can the design of effective reforms progress to the next stage.

## **Working on Design Principles**

That "next stage" is a critical one, for having established the conceptual foundations for understanding the design of governance and its associated regimes, we will face the task of articulating design principles that can guide the policy reform effort. Some of those principles are already implied in the governance approach and regime frameworks themselves, but others require further articulation and testing before they can prove useful.

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23 E.g., Hofstede 1983, 1993, 1998; Wiener 1988; Dubnick 1996.

The very idea of “design” used here is both analogical and metaphorical. Analogically, we are engaged in a process not unlike that undertaken by designers in a number of fields -- from the artist and craftsman to the architect and engineer. For them, as for us, the task is to develop a plan for putting the material and nonmaterial elements at our disposal to work to achieve some preconceived “notion” in the form of a sculpture, product, house or bridge. Our notions take the form of public policies.

“Policies are the first expressions and guiding images of normative thinking and action,” noted Eric Jantsch. “In other words, they are the spiritual agents of change -- change not only in the ways and means by which bureaucracies and technocracies operate, but change in the very institutions and norms which form their homes and castles” (Jantsch 1970, p. 32). In that sense, design is an appropriate metaphor for the creative act -- the development of “spiritual agents of change” -- that the process involves. This is captured by the very concept of policy analysis as a “design science” (Lasswell 1970; also Dror 1971) which seems oxymoronic at first. What bridges the art and science are those principles that guide the design project.

For present purposes, design principles are of three types: logical, conceptual and strategic. In this paper, the principles related to the logic of policy reform are reflected in the governance perspective offered earlier. Reform of a policy domain such as the financial markets can be approached through a variety of logics, each reflecting a general theoretical perspective that might be regarded as little more than a particular (albeit more structured and formalized) view of some participants in the blame game (cf Light 1997). From economists we have a plethora of such logics [e.g., drawn from basic market failure (Bator 1958; Davis & Hulett 1977)<sup>24</sup> and rational expectation theories (Muth 1961; Corsetti, Pseni & Roubini 1999), to those stressing more popular insights regarding “animal spirits” (Akerloff & Shiller 2009) and irrational exuberance (Shiller 2005)]. From the world of political science emerges the logic of various “regulatory capture” (see Mitnick 1980) and other “government failure” theories (Tullock, Seldon & Brady 2002). The perspective offered here focuses on the notions of governance (mostly drawn from the study of public management reform) and regimes (from the study of international organizations), but also relies on the work of economic sociologists and critical theorists who emphasize the importance of governmentality (from the work of Michel Foucault)(Burchell, Gordon & Miller 1991; Bevir 1999; Sending & Neumann 2006) and embeddedness.<sup>25</sup>

Although the logic of governance reform was generally touched upon here, much of this paper has been explicitly devoted to dealing with the conceptual “principles” that emerged from the framing of the regimes. By positing an alternative conceptualization of accountability as a regime, I am (by implication)

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24; However, see Zerbe & McCurdy 1999, 2000.

25 The concept was initially articulated by Karl Polanyi 1944, but today is most often associated with the work of Granovetter 1985, 1992; also see Knippner 2004.

offering a normative reordering of what constitutes the operations of governance of (and through) responsible action within the policy domain.

Despite seeming more like firm directives, the strategic aspect of policy design principles are perhaps best regarded as working hypotheses -- ideally in the form of testable assumptions -- that attempt to apply the logic and conceptual elements of the reform effort to the problematic domain.

Design principles applicable to exclusively to the regulatory regime have been presented in a variety of forms depending on the goal of the presenter. For some it is a matter of designing policies that are more likely to pass muster with policymakers. The guidance they offer is addressed to the rule-designing staff of regulatory agencies and are typically more oriented to meeting political requirements than to developing effective solutions to governance problems. For them the design principles include

- clarity and precision of legislation,
- adherence to the general objects and spirit of the empowering
- legislation,
- not unduly trespassing on personal rights and liberties,
- not reversing the onus of proof in criminal proceedings, and
- ensuring protection from self-incrimination (Coghlan 2003, p. 16).

Policy analysts who take a less politically sensitive approach to regulatory design typically work within some variation of the following principles:

- setting down different types of 'regulation',
- considering if, and when, governments should regulate,
- deciding what forms of government action might best be adopted, and
- examining features that characterise poor or ineffective regulation (Coghlan 2003, p. 16).

More common among economists who approach the design problem as policy analysis but with a focus on what will work for the regulated (as opposed to the politicians) are principles similar to the following offered by Sappington for designing "incentive"-based regulations:

1. Use incentive regulation to better employ the firm's superior information.
2. Prioritize regulatory goals and design incentive regulation to achieve stated goals.
3. Link the firm's compensation to sensitive measures of its unobserved activities.
4. Avoid basing the firm's compensation on performance measures with excessive variability.

5. Limit the firm's financial responsibility for factors beyond its control.
6. Adopt broad-based performance measures where possible, unless their variability is excessive.
7. Choose exogenous performance benchmarks.
8. Allow the firm to choose among regulatory options, while recognizing the interdependencies among the regulatory options that are offered to the firm.
9. Promise only what can be delivered, and deliver whatever is promised.
10. Plan for the rare, unforeseen event, but minimize after-the-fact adjustments to the announced regulatory policy (Sappington 1994, p. 269).

Proffered as advice to policymakers, these design principles are stated in simple terms but underlying them are difficult challenges reflecting the complex combination of logics, concepts and strategic norms. Some of these principles can be translated and transposed to the task of formulating policy options to change the accountability regime, but not without some conceptual and theoretical costs. Care must be taken in developing design principles relevant to the reform of accountability.

While this project is not at the stage where design principles can be pithily summarized in short bullet point statements or sentences, some basic points have emerged that are indicative of the kinds of principles which are likely to emerge. Here are offered three examples:

*Example 1: Reforms of global financial markets must address problems of governance within and across relevant policy domains.*

This principle can easily be transformed into a question: does the proposed policy address governance problems associated with the challenges of control and responsibility? The importance and necessity of this principle becomes obvious at a number of points. It is not uncommon for those engaged in the policy design process to find themselves enthralled with a particular policy approach or instrument, to the point that he or she might lose sight of the policy objective. It is also within the nature of the policy-making and policy legitimation processes that compromises intended to guarantee passage can effectively divert or replace key elements of the reform proposal. A demand for greater discretion by the target population might be necessary for getting the policy adopted, but the policy should be designed to prevent that provision from emasculating the reform effort. Critics of both the recent bank bailouts and the economic stimulus packages have noted the conflicts and flaws that emerged overtime with both policies, but that is to be expected of such emergency measures. But in a highly fragmented policy-making system such as the US where partisan divides remain strong, adhering to this design principle is likely to prove difficult at best.

*Example 2: Governance involves two interrelated functions: establishing control and facilitating responsible action within the policy domain. The efforts made to fulfill both functions are manifest in governance regimes. The operations of the two regimes should be regarded as complementary.*

This principle combines logical, conceptual and strategic guidance. The “bottom line” is highlight the complementarity of the two regimes. This point emerges from the lessons of more myopic governance reforms in financial markets over the past three decades which can be, in turn, related to the current crisis. From the early 1980s, banking reforms in the US and abroad have been characterised as “deregulatory” when seen from the narrow perspective of the regulation regime side of governance. The term “deregulation” is, in fact, a misnomer,<sup>26</sup> for what occurred was a reform of the governance arrangements under which banks operated. What took place has been more appropriately termed a “liberalisation” and/or harmonisation of the regulatory regime that governed the financial sector.<sup>27</sup> The results were a slow but thorough loosening of the control features of domestic, translation and international regulatory regimes.

Under the governance perspective offered here, one can argue that the lack of complementary adjustments in relevant accountability regimes has proven central to creating the current repression. Good governance does not necessarily require an optimal balance between control and responsibility, but too great a gap between the two regimes created by ill advised reforms can certainly generate systemic dysfunctions similar to those we now endure.

*Example 3: The values guiding the two regimes can differ. While regulatory control has primarily instrumental value, the facilitation of responsibility fostered by the accountability regime can have both instrumental and intrinsic value.*

There are cases where the exercise of control over the financial sector has been undertaken for purposes other than the need for more effective governance of that domain, but rarely is regulatory control assumed to hold some intrinsic value. Expropriation of banks for the purpose of fulfilling an ideological or nationalistic program (Trotsky 1938; Lewis 1985) notwithstanding, regulatory regime actions should be described and assessed according to their instrumental value.

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26 Similarly, the term “re-regulation” would not suffice since it implies a deregulation effort preceding it.

27 Majone 2009; Underhill 1991; Claessens, Underhill & Zhang 2008; Underhill & Zhang 2008; Simmons 2001; Pan 2003; Abiad & Mody 2005; Giannetti 2007.

In contrast, while accountability regimes serve instrumental purposes, their role in governance may be or intrinsic value. Thus, a policy that seemingly has no substantial instrumental value at all such as the required restrictions on executive pay, does play a role in enhancing the public perception of a more accountable banking sector, and therefore indirectly achieve an objective of governance reform: e.g., increasing confidence in the banking sector. Or consider the value of policies insuring bank deposits which, on the one hand, play an instrumental role in the regulatory regime as a means for assuring bank solvency, while on the other hand being value for enhancing accountability and an accompanying sense of bank security and integrity. While critics of the policy note moral hazards created by the insurance (and thus question its instrumental value; see Wheelock & Kumbhakar 1995; also O'Driscoll 1988), their concerns are determined to be more than offset by the benefits generated by the assumed enhancement of integrity fostered by responsible behaviour of the insured bank.

## **Concluding comments**

The task that initiated this project was to address the current financial crisis as a policy design problem, and the intent was to develop some reasoned and reasonable paths to reform. “What is to be done!” is the question of the hour, and most responses have unfortunately relied on the usual bag of policy tricks that many regard as merely spot repairs that will keep the system going for long enough to get to the next crisis. It is, as noted earlier, a good example of the “garbage can model” at work: streams of problems, policy solutions and political demands converge at some point and some form of policy emerges from the mix. At times we get lucky and the process works -- producing policies that satisfy our needs for at least a short term resolution. If we are really fortunate, that solution sticks for an extended period.

That seems to be the situation we face at the moment concerning reform of the financial services market. At present, policymakers are relying on the advice given by analysts who specialise in policy repairs and quick fixes rather than policy design. The reasons are many, but they certainly include significant time pressures as well as the dynamics of the blame game which offers up all sorts of targets for so-called reform policies.

To engage in a more substantial policy design effort under crisis conditions might be regarded as a waste of time and energy. Significant policy design requires a critical rethinking of how we approach the collapse of the financial markets and the subsequent damage it caused to economic stability and the possibility of economic growth. At the earliest stages of the design effort, description and theorising about the problem take priority over when the primary goal is to establish an understanding of the domain and its problems. At that stage it is difficult to pull back from the demands for more than mere analysis. Richard Posner, the polymath who combines his full-time position as a major American jurist with his work as a well known public intellectual, published a careful and thoughtful examination of the

crisis in the spring of 2009 and maintained an ongoing discussion of his views on a widely read blog.<sup>28</sup> Pushed to suggest long term solutions, he steadfastly refused, noting that it is too early to make suggestions that matches his assessment that there is something fundamentally wrong with the US economy. He is, in that sense, the model policy designer.

I approach the present project with a similar perspective, engaging in a critical (and time consuming) rethinking of the way we approach the problems of the financial markets and attempting to construct a framework that might prove useful in developing a long term strategy for reform of that sector. What I have provided here is a perspective emphasising the central role that governance plays in this policy domain, and an attempt to make the case for a more balanced approach to governance that encompasses the need for greater accountability as well as more regulatory control. Emulating the work of Hood, Rothstein and Baldwin on regulatory regimes, I have presented the basic framing for understanding accountability regimes. And although that part of the project remains to be completed, I have also addressed the need for policy design principles that reflect the complex nature of the governance arrangements that are in need of major reform.

More work remains to be done.

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28 The blog was located at [http://correspondents.theatlantic.com/richard\\_posner/](http://correspondents.theatlantic.com/richard_posner/)

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