

Braithwaite, John

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RESPONSIVE REGULATION AND DEVELOPING ECONOMICS

John Braithwaite,

Professor, The Australian National University

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John Braithwaite

John Braithwaite is a Professor at the Research School of Social Sciences, Australian National University. He works on business regulation and criminal justice, and particularly on restorative justice. His recent publications include: *Not Just Deserts: A Republican Theory of Criminal Justice* (1990, with Philip Pettit); *Responsive Regulation: Transcending the Deregulation Debate* (1992, with Ian Ayres); *Business Regulation and Australia's Future* (1993, edited with Peter Grabosky); *Corporations, Crime and Accountability* (1993, with Brent Fisse); *Global Business Regulation* (2000, with Peter Drahos); and *Regulation, Crime and Freedom* (2000).

Braithwaite served part-time on the Trade Practices Commission (1985 - 1995) and on the Economic Planning Advisory Council, chaired by the Prime Minister (1983 - 1987). He has won a number of international prizes for his work on crime from the American Society of Criminology, the Society for the Study of Social Problems, the Institute for Financial Crime Prevention and the Socio-Legal Studies Association.

Summary

Developing states with limited regulatory capacity might benefit from a responsive approach to regulation. Responsive regulation is a democratic ideal, incorporating notions of deliberative democracy and restorative justice. Responsive regulation conducted by regulatory networks of governmental and non-governmental actors allows for networking around capacity deficits. NGOs play a vital role in this kind of regulation. By utilizing NGOs and local social pressure, developing countries might develop a 'regulatory society' model, bypassing the regulatory state. Where capacity remains limited, private bounty hunting (such as fees for successful private prosecutions) may become an appealing tool for achieving certain regulatory objectives.

1. Introduction¹

Responsive regulation is an approach designed in developed economies (Ayres & Braithwaite, 1992). Most of the critiques of it are also framed within the context of developed economies (Black, 1997; Gunningham & Grabosky, 1998; Haines, 1997; but see Haines, 2003). This essay addresses the limitations of responsive regulation as a strategy in developing economies and poses some solutions to those limitations. First it is argued that developing countries mostly have less regulatory capacity than developed ones. Yet herein also lies some of the potential of responsive regulation for developing countries as a strategy that mobilizes cheaper forms of social control than state command and control. Nevertheless, responsive regulation does require a big stick at the peak of an enforcement pyramid and big sticks are expensive, as well as demanding upon state capacities in other ways.

Two new strategies of networked governance are then developed for networking around these capacity deficits. One is based on pyramidal escalation of network branching. The second is legislating for *qui tam* actions (bounty hunting by whistle blowers). When public enforcement fails to take charge, the *qui tam* alternative is private markets in bounty hunting where a whistle blower (usually someone at a senior level inside a law-breaking organization who knows what is going on) prosecutes and claims 25% of a regulatory penalty. Before considering responsiveness as an ideal for developing countries, the opening section of the paper considers responsiveness as a democratic ideal.

2. Responsiveness as a Democratic Ideal

For Philip Selznick (1992, p.336), the challenge of responsiveness is “to maintain institutional integrity while taking into account new problems, new forces in the environment, new demands and expectations”. This means responsiveness becomes a democratic ideal - responding to peoples’ problems, environments, demands: “responsiveness begins with *outreach* and *empowerment*...The vitality of a social order comes from below, that is, from the necessities of cooperation in everyday life” (Selznick, 1992, p.465). Responsiveness means having respect for the integrity of practices and the autonomy of groups; responsiveness to “the complex texture of social life” (Selznick, 1992, p.470). Tom Paine in the *Rights of Man* and James Madison share with Selznick the project of conceiving empowered civic virtue as at least as important to democracy as constitutional checks and balances: “power should check power, not only in government but in society as a whole” (Selznick, 1992, p.535). So, for example, business custom shapes responsive business regulatory law and state regulators check

¹ I owe an unusually heavy debt in this work to four co-authors of mine. Ian Ayres, Peter Drahos, Brent Fisse and Christine Parker have stimulated all the foundations on which this essay is built. My thanks also to Cecily Stewart and Sascha Walkley for research assistance with a creative edge and to Hilary Charlesworth, David Graham, David Levi-Faur, Christine Parker, Rod Rhodes, Declan Roche, and Ngaire Woods for invaluable comments on an earlier draft.

abuse of power in business self-regulatory arrangements, and both should have their power checked by the vigilant oversight of NGOs and social movements.

Developing countries mostly have less oversight by NGOs and social movements to mobilise, less state regulatory capability and less settled, less powerful, business custom, at least in the larger business sector. Restorative and responsive regulatory theory has evolved into a deliberative, circular theory of democratic accountability, as opposed to a hierarchical theory where the ultimate guardians of the guardians are part of the state (Braithwaite, 2002; Braithwaite & Roche, 2000). This ideal is for guardians of accountability to be organized in a circle where every guardian is holding everyone else in the circle accountable, where each organizational guardian holds itself internally accountable in deliberative circles of conversation and where such circles are widened when accountability fails - circles of widening deliberative circles. Rules remain important under a restorative and responsive model of democratic accountability, but less important than under Dicey's hierarchical accountability up to a sovereign parliament. Rules are just one of the things that emerge from the circled circles of deliberation. Another is the interpretation of rules – interpretation comes from circles of conversation in which courts might be particularly influential, but where the interpretations that matter mostly do not come down from a court or a canonical papal interpretation of God's will.

In this regard my conception of responsiveness differs from Gunther Teubner's (Teubner, 1986) reflexiveness and Niklas Luhmann's autopoiesis (Teubner, 1988). I do not see law and business systems as normatively closed and cognitively open. In a society with a complex division of labour the most fundamental reason social systems are not normatively closed is that people occupy multiple roles in multiple systems. A company director is also a mother, a local alderman and a God-fearing woman. When she leaves the board meeting before a crucial vote to pick up her infant, her business behaviour enacts normative commitments from the social system of the family; when she votes on the board in a way calculated to prevent defeat at the next Council election, she enacts in the business normative commitments to the political system; when she votes against a takeover of a casino because of her religious convictions, she enacts the normative commitments of her church. In extremis, wealthy business people sometimes dismantle their empires to give away their wealth for a charitable foundation. So much of the small and large stuff of organizational life makes a sociological nonsense of the notion that systems are normatively closed. Nor is it normatively desirable that they be normatively closed, as Christine Parker (2002) has argued. Rather, there is virtue in the justice of the people and of their business organizations bubbling up into the justice of the law, and the justice of the law percolating down into the justice of the people and their commerce.

That said, responsive and reflexive regulatory theories are mostly on the same wavelength. Teubner's regulatory trilemma is a real one (Teubner, 1986). A law that goes against the grain of business culture risks irrelevance; a law that crushes normative systems that naturally emerge in business can destroy virtue; a law that lets business norms take it over can destroy its own virtues. I am at one with Teubner in seeing it as essential to regulate by working with the grain of naturally occurring systems in business (Braithwaite, 2005a, ch.13). We agree that it is through the "structural coupling" of

reflexively related systems (or nodes of networked governance as I would prefer) that the horns of the regulatory trilemma can be escaped. Abuse of power is best checked by a complex plurality of many separated powers – many semi-autonomous nodes of networked governance (Braithwaite, 1997, pp.311-13; Braithwaite, 2005b). All nodes of separated private, public or hybrid governance need enough autonomy so that other nodes of governance cannot dominate them. Equally, each needs enough capacity to check abuse of power by other nodes so that a multiplicity of separated powers can network to check any node of power from dominating all the others. The required structural coupling among a rich plurality of separated powers is not only about checking abuse, it is also about enhancing the semi-autonomous power of nodes of governance to be responsive to human needs (Teubner, 1986, pp.316-318).

Nodes of governance must not only check one another's abuses, they must also assist with building one another's capacity to responsively serve human needs, to have integrity in Selznick's terms (Selznick, 1992). A regulatory node can do this, for example, through assisting build the learning capacity of a business node to solve its environmental problems. The same idea is found in Habermas (1987) where on the one hand he notes the dangers of law as "medium" which colonizes the lifeworld, and on the other hand notes the virtues of law as "constitution" which enables the lifeworld to more effectively deliberate solutions to problems that are responsive to citizens.

Circled circles of guardians can include audit offices, ombudsmen, appellate courts, public service commissions, self-regulatory organizations, ministers and NGOs. But again the deliberative capacities of all such kinds of actors tend to be less in developing economies. Responsiveness is enabled by a society with a strong state, strong markets and strong civil society, where the strength of each institution enables the governance capabilities of the other institutions (Braithwaite, 1998). Developing countries have weaker markets that hold back the development of state capacity and a weaker state that holds back the development of all other institutions (Evans, 1995), including the institutions of civil society that can compensate for the failures of states.

From a responsiveness perspective, it follows that economies with developed, well-funded, institutions of guardianship enjoy a richer democracy than nations that cannot afford them. On the other hand, responsive regulatory theory offers a more useful theory of "what is to be done" in developing countries than statist theories. If we believe that democracy is fundamentally an attribute of states, when we live in a tyrannous state or a state with limited effective capacity to govern, we are disabled from building democracy – we are simply shot when we try to, or we waste our breath demanding state responses that it does not have the capacity to provide. But when our vision of democracy is messy - of circles of deliberative circles, there are many kinds of circles we can join that we believe actually matter in building democracy. Democracy is then not something we lobby for as a distant utopia when the tyrant is displaced by free elections, democracy is something we start building as soon as we join the NGO, practice responsively as a lawyer, establish business self-regulatory responses to demands from environmental groups, deliberate about working conditions with our employees or employers, educate

our children to be democratic citizens, participate in a global conversation on the internet, and so on.

3. Responsiveness as an Effectiveness Ideal

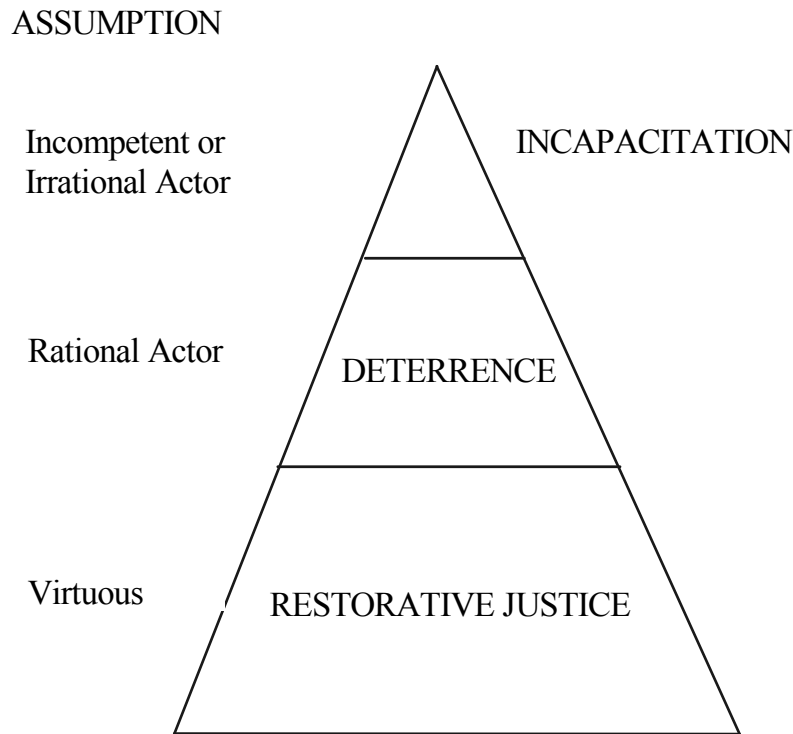
The basic idea of responsive regulation is that governments should be responsive to the conduct of those they seek to regulate in deciding whether a more or less interventionist response is needed (Ayres & Braithwaite, 1992). In particular, law enforcers should be responsive to how effectively citizens or corporations are regulating themselves before deciding whether to escalate intervention. The most distinctive part of responsive regulation is the regulatory pyramid. It is an attempt to solve the puzzle of when to punish and when to persuade. At the base of the pyramid is the most deliberative approach we can craft for securing compliance with a just law. Of course if it is a law of doubtful justice, we can expect the dialogue to be mainly about the justice of the law (and this is a good thing from a democratic perspective). As we move up the pyramid, more and more demanding interventions in peoples' lives are involved. The idea of the pyramid is that our presumption should always be to start at the base of the pyramid first. Then escalate to somewhat punitive approaches only reluctantly and only when dialogue fails. Then escalate to even more punitive approaches only when the more modest forms of punishment fail.

The crucial point is that it is a dynamic model. It is not about specifying in advance which are the types of matters that should be dealt with at the base of the pyramid, which are the more serious ones that should be in the middle and which are the most egregious ones for the peak of the pyramid. Even with the most serious matters – flouting legal obligations to operate a nuclear power plant safely that risks thousands of lives - we stick with the presumption that it is better to start with dialogue at the base of the pyramid (see Rees, 1994). A presumption means that however serious the lawbreaking, our normal response is to try dialogue first for dealing with it, to only override this presumption if there are compelling reasons for doing so. As we move up the pyramid in response to a failure to elicit reform and repair, we often reach the point where finally reform and repair is forthcoming. At that point responsive regulation means that we put escalation up the pyramid into reverse and de-escalate down the pyramid. The pyramid is firm yet forgiving in its demands for compliance. Reform must be rewarded just as recalcitrant refusal to reform will ultimately be punished.

Responsive regulation has been an influential policy idea because it comes up with a way of reconciling the clear empirical evidence that sometimes punishment works and sometimes it backfires, and likewise with persuasion (Braithwaite, 1985; Ayres & Braithwaite, 1992). The pyramidal presumption of persuasion gives the cheaper and more respectful option a chance to work first. The more costly punitive attempts at control are thus held in reserve for the cases where persuasion fails. When persuasion does fail, the most common reason is that a business actor is being a rational calculator about the likely costs of law enforcement compared with the gains from breaking the law. Escalation through progressively more deterrent penalties will often take the rational calculator up to the point where it will become rational to comply. Quite often, however, business

regulators find that they try dialogue and restorative justice and it fails; they try escalating up through more and more punitive options and they all fail to deter. Perhaps the most common reason in business regulation for successive failure of restorative justice and deterrence is that non-compliance is neither about a lack of goodwill to comply nor about rational calculation to cheat. It is about management not having the competence to comply. The manager of the nuclear power plant simply does not have the engineering knowhow to take on a level of responsibility this demanding. He must be moved from the job. Indeed if the entire management system of a company is not up to the task, the company must lose its licence to operate a nuclear power plant. So when deterrence fails, the idea of the pyramid is that incapacitation is the next port of call (see Figure 1).

Figure 1: Toward an Integration of Restorative, Deterrent and Incapacitative Justice



This design responds to the fact that restorative justice, deterrence and incapacitation are all limited and flawed theories of compliance. What the pyramid does is cover the weaknesses of one theory with the strengths of another. The ordering of strategies in the pyramid is not just about putting the less costly, less coercive, more respectful options lower down in order to save money. It is also that by only resorting to more dominating, less respectful forms of social control when more dialogic forms have been tried first, coercive control comes to be seen as more legitimate. When regulation is seen as more legitimate, more procedurally fair, compliance with the law is more likely (Tyler, 1990; Tyler & Dawes, 1993; Tyler & Blader, 2000; Tyler & Huo, 2001). Astute business regulators often set up this legitimacy explicitly. During a restorative justice

dialogue over an offence, the inspector will say there will be no penalty this time, but that she hopes the manager understands that if she returns and finds the company has slipped back out of compliance again, under the rules she will have no choice but to shut down the production line. When the manager responds yes this is understood, a future sanction will likely be viewed as fair. Under this theory, therefore, privileging restorative justice at the base of the pyramid builds legitimacy and therefore compliance.

There is also a rational choice account of why the pyramid works. System capacity overload (Pontell, 1978) results in pretence of consistent law enforcement where in practice enforcement is spread around thinly and weakly. Unfortunately this problem will be at its worst where lawbreaking is worst. Hardened offenders learn that the odds of serious punishment are low for any particular infraction. Tools like tax audits that are supposed to be about deterrence are frequently exercises that backfire by teaching hardened tax cheats just how much they are capable of getting away with (Kinsey, 1986, p.416). The reluctance to escalate under the responsive pyramid model means that enforcement has the virtue of being highly selective in a principled way. Moreover the display of the pyramid itself channels the rational actor down to the base of the pyramid. Non-compliance comes to be seen (accurately) as a slippery slope that will inexorably lead to a sticky end. In effect what the pyramid does is solve the system capacity problem with punishment by making punishment cheap. The pyramid says unless you punish yourself for lawbreaking through an agreed action plan near the base of the pyramid, we will punish you much more severely higher up the pyramid (and we stand ready to go as high as we have to). So it is cheaper for the rational company to punish themselves (as by agreeing to payouts to victims, community service, paying for new corporate compliance systems). Once the pyramid accomplishes a world where most punishment is self-punishment, there is no longer a crisis of the state's capacity to deliver punishment where it is needed. One of the messages the pyramid gives is that "if you keep breaking the law it is going to be cheap for us to hurt you because you are going to help us hurt you" (Ayres & Braithwaite, 1992, ch.2.)

This feature of the theory of responsive regulation is attractive for developing countries. Precisely because responsive regulation deals with the fact that no government has the capacity to enforce all laws, it is useful for thinking about regulation in developing countries with weak enforcement capabilities. Yes certain minimum capacities must be acquired, but then the theory shows how such limited capacity might be focused and leveraged.

Paternoster and Simpson's research on intentions to commit four types of corporate crime by MBA students reveals the inefficiency of going straight to a deterrence strategy (Paternoster & Simpson, 1996). Paternoster and Simpson found that where the MBAs held personal moral codes, these were more important than rational calculations of sanction threats in predicting compliance (though the latter were important too). It follows that for the majority of these future business leaders, appeals to business ethics (as by confronting them with the consequences for the victims of corporate crime) will work better than sanction threats. So it is best to try such ethical appeals first and

then escalate to deterrence for that minority for whom deterrence works better than ethical appeals.

Because states are at great risk of capture and corruption by business, even greater risk where regulatory bureaucrats are poor, Ayres and Braithwaite argue for the central importance of third parties, particularly NGOs, to be directly involved in regulatory enforcement oversight (Ayres & Braithwaite, 1992, ch.3). But NGOs do more than just check capture of state regulators; they also directly regulate business themselves, through naming and shaming, restorative justice, consumer boycotts, strikes and litigation they run themselves. Responsive regulation comes to conceive of NGOs as fundamentally important regulators in their own right, just as business are important as regulators as well as regulates (see also Gunningham & Grabosky, 1998; Parker, 2002).

Pyramid design is a creative, deliberative activity. Stakeholders can design pyramids of actual sanctions like a “warning letter” or “civil penalty”. Or they can design a pyramid of regulatory strategies – for example, try regulation by the price mechanism of the free market first, then try industry self-regulation, then a carbon tax regime, then a command and control regime that permits licence revocation for power plants that fail to meet pollution reduction targets. Regulators that think responsively tend to design very different kinds of pyramids for different kinds of problems – for example the Australian Taxation Office has a different kind of pyramid for responding to transfer pricing by multinational companies than it deploys with the same companies when they “defer, delay and deny” access to company records (Braithwaite, 2005a, part II).

As with responsiveness as a democratic ideal, so with responsiveness as an effectiveness ideal, the theory appears to be one where developing countries are less likely than wealthy states to enjoy the conditions to make it work. Not only are state regulatory bureaucrats more vulnerable to corruption because of their poverty, NGOs have fewer resources to do the oversight to guard against this than do NGOs in rich nations. More fundamentally, weaker states lack the organizational capacity to be responsive. They have fewer regulatory staff and less educated staff to come to grips with the more reflexive approach of responsive regulation. Perhaps factory inspectors in weak states do have the capacity for some of the more important kinds of command and control regulation like ensuring that hazardous machinery is guarded, but they are less like to have the analytic resources to assess a “safety case” – an occupational health and safety self-regulatory plan. Developing country tax officials might do quite well at taxing immobile assets like land, but may not have enough highly educated staff to implement responsive regulatory strategies that states like Australia can use against international profit shifting to recover a billion dollars in avoided tax for every million dollars spent on the enforcement (Braithwaite, 2005a, ch.6)

Empirical studies of developing states show great variation in state capacity (see, for example, Evans, 1995; Kohli, 2004). While in general Peter Evans does not find the problem of developing economies as too much bureaucracy, but of not enough, he discerns huge differences between predatory states like Mobutu’s Zaire where bureaucratic competence is systematically destroyed, developmental states such as Korea

where it is nourished, and in-between states such as India and Brazil where state capacity in the early 1990s was uneven, but where bureaucratic learning and construction of state capacity did occur (Evans, 1995, pp.12-70).

4. Networking Around Capacity Deficits

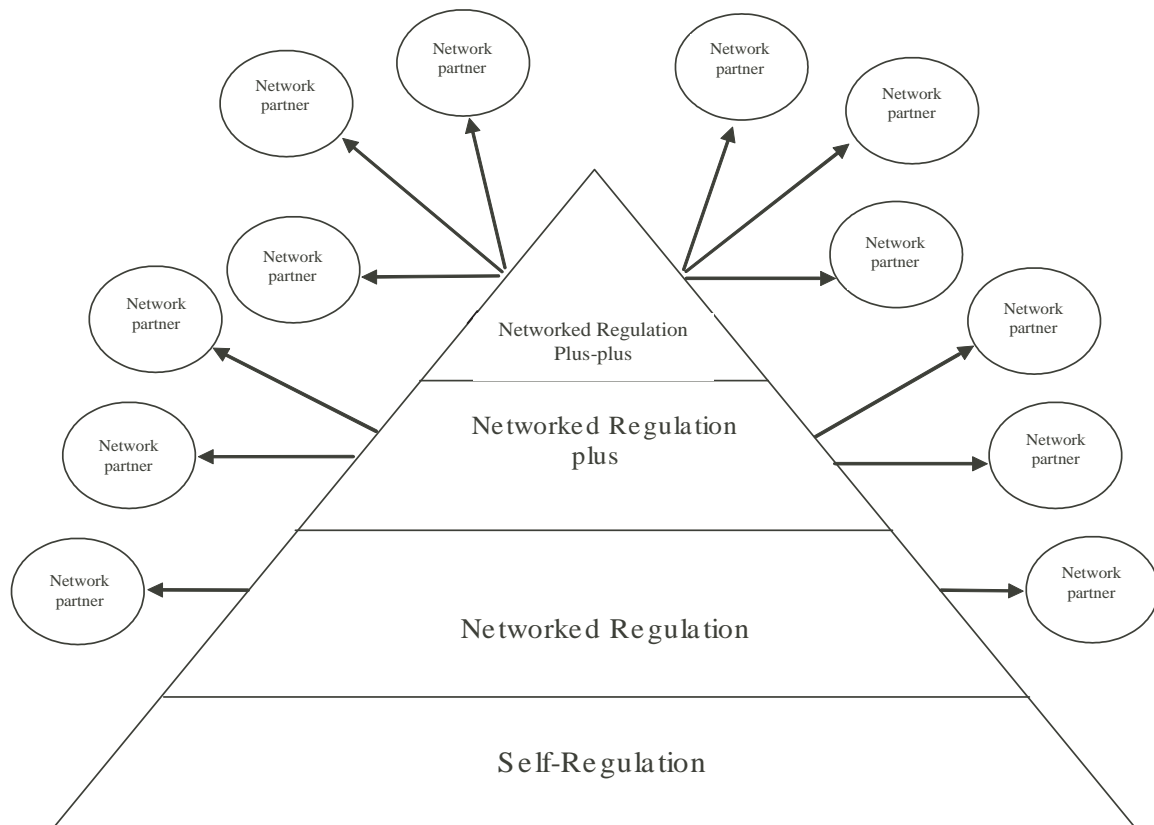
Braithwaite and Drahos (2000) concluded from their interview-based research that the most important regulators of corporate fraud and accounting standards in developing economies were the major global accounting firms. In comparison, developing country corporations and securities regulators mostly have very limited standard setting capability, let alone enforcement capability. Professions and other non-state gatekeepers did more of the regulating of business in what are today developed economies as we go back through their histories to when they were developing economies. Even in the United States we only need to go back to the 1920s for a pre-SEC world where accountants and private partnerships called stock exchanges did all the work that mattered in the regulation of corporations, securities and accounting standards (McCraw, 1984)¹. Until quite late in the twentieth century, the city of London flourished through a gentlemen's club model of regulation, where accounting standards that entered commerce through the accounting profession were internalised by "decent chaps" who learnt the standards they had to meet to avoid being ostracized to the margins of the City's circles of gentlemen (Clarke, 1986; Moran, 2003). Arguably it was only in the twentieth century that the Bank of England became a more important prudential regulator than the Rothschilds, that JP Morgan ceased being the most important prudential regulator in the United States (Braithwaite & Drahos, 2000, ch.8).

For many decades after the West's industrial revolution began, we see very different ways in different metropolises that regulation is networked by a plurality of private, professional and state actors. Only slowly after the New Deal do we see the transformation of regulatory thinking to the ideal of a state regulator being ultimately in charge of a regulatory domain. No sooner had this transformation been consolidated when what some like to refer to as a post-regulatory state (Teubner, 1986; Scott, 2004)² began to develop – a social order where regulation pluralizes again as NGOs find new capacities and competition policy drives professions to innovate into new markets in regulatory evasion and new markets in private regulation of such evasion ("markets in vice, markets in virtue") (Braithwaite, 2005a). Law firms that specialize in product liability litigation become important new regulators of business, NGO environmental regulators form partnerships with retailers to regulate the certification of forest products or the certification of coffee as organically grown (Courville, 2003). Transparency International regulates corruption through publicising where high levels of corruption prevail, as do ethical investment funds and their analysts. New kinds of ratings agencies like Reputex rate corporate social responsibility (Reputation Measurement, 2003). Indeed the older ratings agencies like Moodys and Standards and Poors are becoming increasingly important regulatory threats to businesses with major environmental and ethical risks to their operations that can peg back their credit rating. Finally, international regulators such as the Basle committee, environmental treaty secretariats and the International Telecommunications Union become increasingly important. Braithwaite and

Drahos (2000) conclude that in shipping regulation and some other domains, the era when state regulators are more in charge than private regulators, such as Lloyds of London, and global ones such as the International Maritime Organization, is remarkably short. Anne-Marie Slaughter (2004) sees regulation as the area where transgovernmental networks become pre-eminently important as fonts of governance.

Like Slaughter (2004), Castells (2000a, 2000b, & 2000c), Drahos (2004), Rhodes (1997; Bevir & Rhodes, 2003) and others, I have become persuaded that we live in an era of networked governance. An implication of this is that developing countries might jump over their regulatory state era and move straight to the regulatory society era of networked governance. Developing states might therefore cope with their capacity problem for making responsive regulation work by escalating less in terms of state intervention and more in terms of escalating state networking with non-state regulators. Figure 2 represents this idea, which comes from Peter Drahos's insight that networked governance could be of service to responsive global regulation that works better for developing countries (Drahos, 2004). At the base of the pyramid, the developing state relies upon business self-regulation. When self-regulation fails, it networks two other non-state regulators. When that fails, it networks two more, and so on.

Figure 2: A Responsive Regulatory Pyramid for a Developing Economy to Escalate the Networking of Regulatory Governance

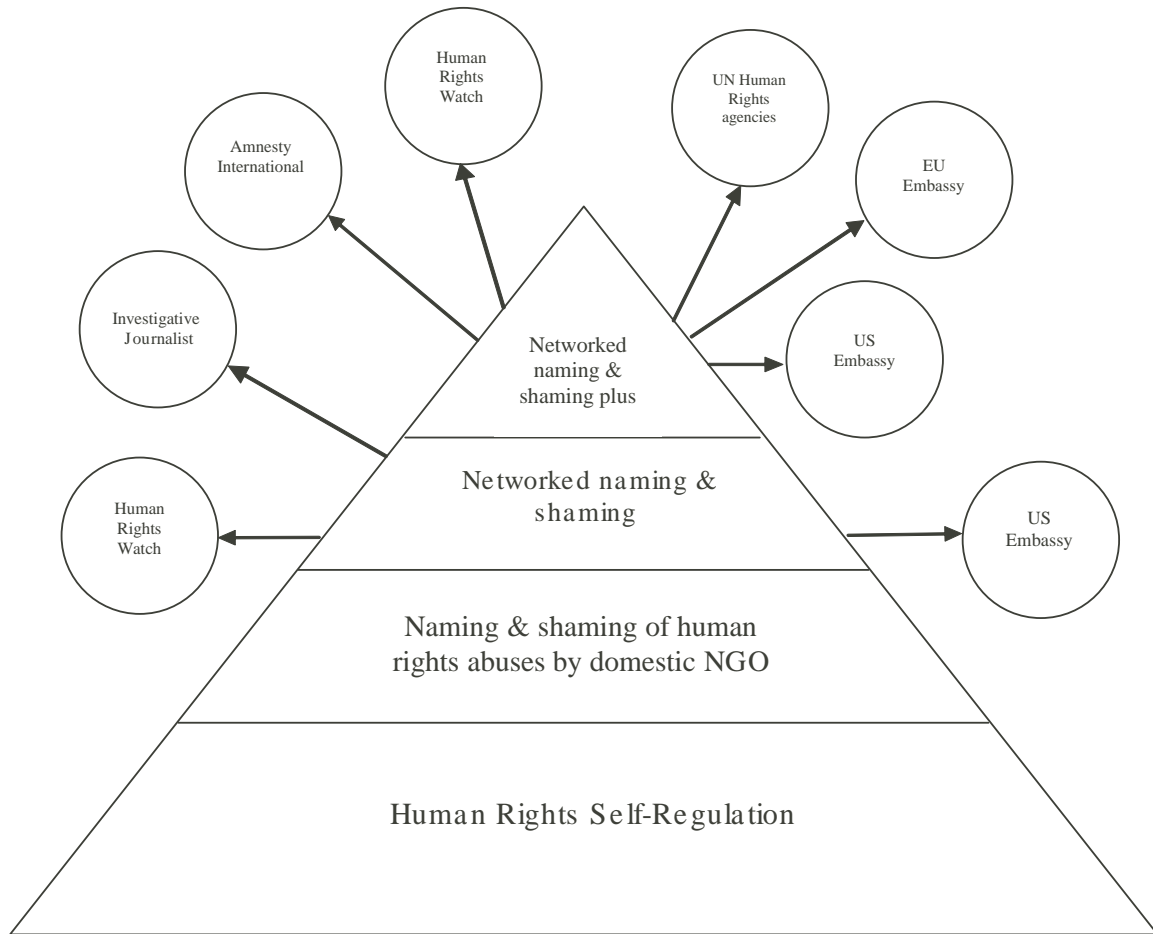


In Figure 2 the developing state enrolls more (Latour, 1986) and more NGOs, industry association co-regulators, professions, other gatekeepers and international organizations to its regulatory project. In addition to such non-state actors it might also enroll other states as regulators within its own boundaries. For example, an Indonesian state with weak capacity to control people smuggling businesses that move desperate people from states such as Afghanistan on boats that stop in Indonesia (often in transit to Australia), enrolls the regulatory and intelligence capabilities of officers of the Australian state based in Indonesia. In some domains of regulatory enforcement, such as that against pirating of intellectual property rights, developing states rely less on state regulators than on foreign enforcers with an interest in the enforcement. In many developing country capitals, the most powerful regulatory agency in town has a red and white striped flag out the front. This kind of regulation is not enacted by a monolithic foreign state, but by functionaries of specific agencies, which are part of the same trans-governmental network as the domestic state regulator. Slaughter (2004) explains that contemporary state power is disaggregated into the hands of distinct regulators and then re-aggregated into trans-governmental networks. The police attaché in a foreign embassy may have more allegiance to some of the domestic police she works with than to her own nation's Ambassador. She may share more secrets with her police network than she would ever share with her ostensible boss, the Ambassador. In extremis, she might even do things like conspire within a trans-national policing and security network in assassination plots aimed at major transnational criminals in circumstances where the Ambassador would view this as abhorrent and unauthorized.

While Slaughter goes too far in conceiving the networks that matter in regulatory space as fundamentally trans-governmental, as opposed to networks of private and public regulators, her empirical assertion that it is regulators from different states who put most of the grunt into such networks is worthy of testing in future research. Moreover her complementary normative claim deserves to be taken seriously and rigorously examined in future normative research. This is the claim that only states, or perhaps only democratic states, are likely to have a claim to the legitimacy to organize trans-national networks in a way that will be accepted as public regarding.

Nevertheless, I expect Anne-Marie Slaughter would concede that there are some developing countries where the most effective regulator of corporate abuses of human rights is an NGO. This is especially likely in one of Peter Evan's "predatory states" that mostly has little interest in securing human rights. One reason that the domestic NGO can be the more potent human rights regulator than the domestic state is that, unlike its state, this NGO is interested in networking with an international NGO that has people on the ground like Human Rights Watch, with UN Human Rights agencies, with the woman in the US Embassy with a watching brief on human rights, investigative journalists and so on. Figure 3 represents the responsive regulatory strategising such an NGO might do to enforce human rights norms.

Figure 3: Regulatory Pyramid for a Developing Country Human Rights NGO Seeking to Escalate Networked Regulation for Human Rights

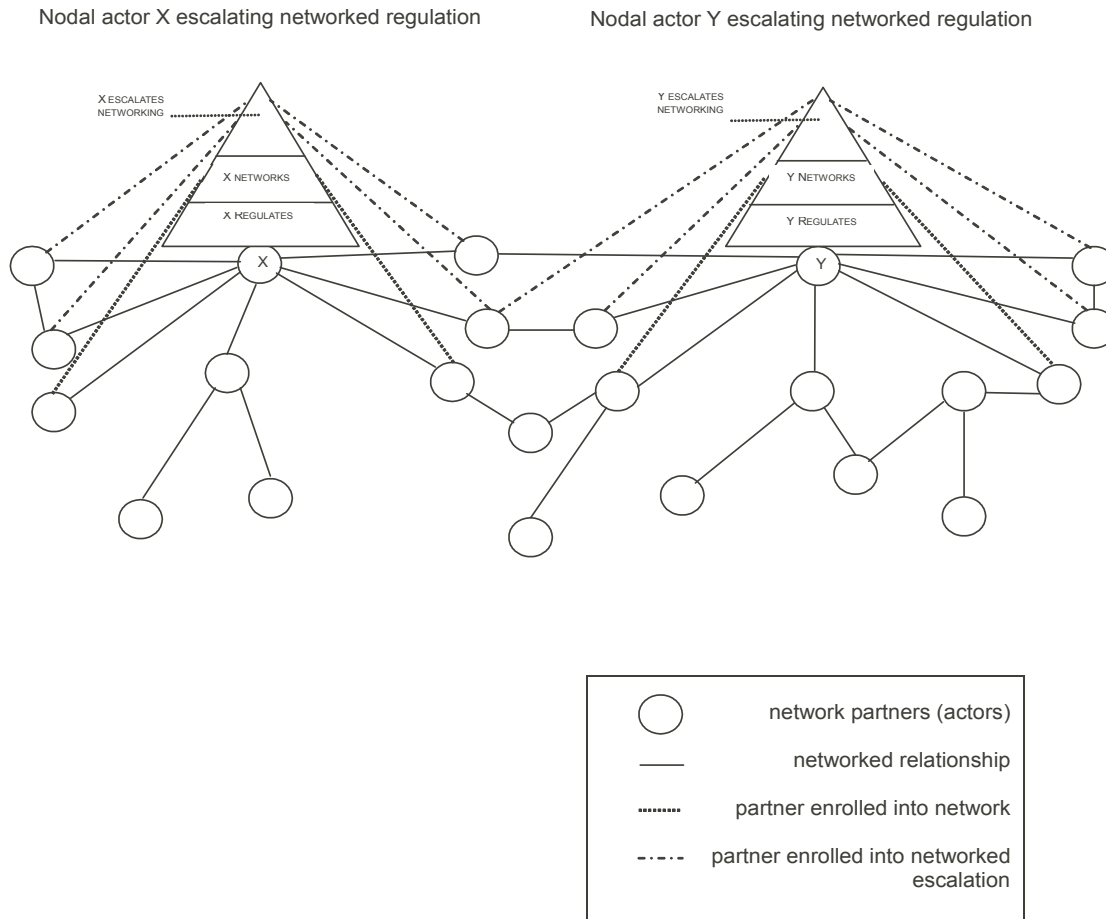


Note that in Figure 3 the NGO as regulator can be conceived as either a regulator of business human rights abuses, or as a regulator of states - either for their failure to regulate corporate human rights abuses or for the state's own abuses. There is of course still a capacity problem in the fact that Figure 3 imagines developing country NGOs as initiators of responsive regulation when we know that NGOs are thinner on the ground than they are in developed economies and more poorly resourced. On the other hand, the evidence is that while NGOs are growing fast in both the developed and developing world, the growth rate is fastest in the developing world (Commission on Global Governance, 1995, p.33). Secondly, the growth of international NGO presence on the ground in developing countries has been considerable in recent decades. Hence, where there is no local human rights NGO, or where all its key players have been murdered, Human Rights Watch might step in to network the naming and shaming, networking with investigative journalists, and to nurture the creation of new domestic human rights NGOs. Either way, it is the networking of responsive escalation that is advanced as a path around the developing economy's capacity problem for enforcing standards.

Obviously, existing networks of governance in many developing countries are more oriented to crushing human rights than to enhancing them. Extant networks of global governance are more oriented to advancing the interests of the G7 and the EU than those of developing nations. Even within developed economies, networked NGO power or the networked governance capabilities of state regulators is often miniscule compared to networked corporate power. But the question of interest here is how a developing nation's regulators, or NGOs with the interests of poor at heart, might act in such a world of networked governance where extant networking favours the rich and the abusers of human rights. The answer proffered is to network. It is that weaker actors can become stronger by networking with other weaker actors. Beyond that, Braithwaite and Drahos (2000) show that the interests of the strong are not monolithic, that the weak can often enrol the power of one strong actor against another. The human rights or environmental NGO can enrol the clout of the European Union against the behaviour of the US or its corporations in developing economies, or the US can be enrolled against the EU (see, for example, Braithwaite & Drahos, 2000, pp.264-7). In a world of networked power, however much or little power you have, the prescription for potency is not to sit around waiting for your own power to grow (by acquiring more wealth or more guns, for example). Rather the prescription is to actively network with those with power you do not yourself control.

Clearly responsively escalating networked regulation is something states can do by enrolling NGOs, and NGOs can do by enrolling state agencies of different kinds. Business actors, like accounting firms regulating corporate accounting standards, can also responsively escalate networked regulation by enrolling state agencies and NGOs. Networked governance is about the observation that all of these kinds of actors do interact in networks and do enrol one another, sometimes in conflicting projects, sometimes in synergy. Figure 4 shows a network of governance actors of these different kinds, where only two of the actors – X and Y – have a sufficiently nodal set of ties to mount a pyramid of escalating networked regulation. The other actors in the network do not have enough links to enrol the networked escalation required for responsive regulation.

Figure 4: A Network of Governance in which Just Two Nodal Actors have a Capacity to Escalate Networked Regulation



Where X and Y have a shared regulatory objective – say improving the integrity of accounting standards or anti-corruption measures in a developing country – the synergies between their regulatory pyramids create the potential for considerable regulatory potency. This potency is based on a redundancy where the weaknesses of a state regulator may be compensated by the strengths of NGO or business regulators. The concomitant danger is that the very sharing of the regulatory objective by the only actors with the capability to escalate networked regulation means that their convergent power may be unchecked.³ If the consensual synergies among different pro-regulation constituencies are excessively hand in glove, over-regulation is a risk.

In developing economies the greater risk is the reverse: big business networked with ruling families dominate an anti-regulation consensus lubricated by bribery and extortion. The civic republican ideal (Pettit, 1997; Braithwaite, 1997 & 1998) is that pro-regulation and anti-regulation actors can both mobilize effective networked escalation as a check on domination by any one form of networked power. When fundamental labour rights are being crushed, the local trade union can escalate up to networked support from a state ministry of labour, the International Confederation of Free Trade Unions, the labour attaché at the US embassy, the Campaign for Labour Rights, the Clean Clothes

Campaign or Oxfam International. When a firm is at risk of being driven out of business by unsustainable demands from a trade union with formidable ability to enrol political elites and industrial muscle, the firm can network escalated resistance from pro-business agencies of the state, industry associations, and the like. The republican ideal is that such contestation should occur to prevent domination; the responsive ideal is that it happens responsively. The combined ideal is that pyramidal escalation to contest domination drives contestation down to the deliberative base of the pyramid, so that regulation is conversational (Black, 1997) rather than based on deterrence or incapacitation (see Figure 1). The capacity of the labour union to escalate to strikes, networked naming and shaming, networked state enforcement, drives the company down to restorative justice at the base of the pyramid. The capacity of the company to escalate to litigation or political pressure to halt the union's tactics drives the union down to negotiated problem solving at the base of the pyramid. Credible capacity of both sides to escalate in ways that threaten win-lose outcomes gives both the incentive to deliberate collaboratively in search of a win-win solution. Of course extant realities of power in any society are unprincipled, fraught with countless dominations of the weak by the strong. The perspective here does no more than supply a perspective on a direction to struggle and a way to struggle, however weak one's constituency, for more principled checking of any and all abuses of power.

The intersection of the theories of networked governance, responsive regulation and republican separations of powers is a fruitful topic for more detailed research, especially for developing economies: "The more richly plural the separations into semi-autonomous powers, the more the dependence of each power on many other guardians of power will secure their independence from domination by one power"(Braithwaite, 1997, p.312). Contrary to Montesquieu's clear conception of a separation of public powers between executive, judiciary and legislature (Montesquieu, 1989), there is virtue in many unclear separations of public and private powers. This republican virtue is especially present where each separated power can enrol others through networks of governance. Regulators have powers separated between the public and the private, within the public and within the private sphere, where separations are many and transcend private-public divides (Braithwaite, 1997). Nodes of governance need to be sufficiently networked to be able to check the power of one node from dominating other nodes of governance.

In developed economies there is what some regulatory scholars call a dual economy (Haines, 1997) where very different regulatory strategies may be required with large business than with small and marginal businesses. In developing economies we need to take this further down to a third village-level informal economy that is typically untaxed and almost entirely unregulated by the state. Village reputation networks often regulate this economy more effectively than the regulation of national companies and multinationals that congregate in the large cities. Village elders may have persuasive means of sitting down local traders in some sort of traditional restorative justice process when, for example, they cheat on weights and measures. This was also true of the 18th century informal "police" of European towns and parishes that we see discussed in the writings of the likes of Adam Smith (Smith, 1978). At the level of national companies in developing economies we hypothesise that national NGOs can sometimes network with

state regulators to improve the responsiveness of regulation. And it is at the level of regulating Northern multinationals that it is hypothesised that international NGOs, disaggregated fractions of Northern states and auditors from the multinational's own corporate headquarters must be enrolled to the (much more difficult) regulatory challenge of exploitation by global corporations.

5. Bounty Hunting Around Capacity Deficits

In 2002 ranking US Republican on the Senate Finance Committee, Charles E. Grassley, called for public disclosure of corporate tax returns (Stratton, 2002, p.220). The call was motivated by the vast difference between the numbers in Enron and WorldCom's tax returns and their financial statements to the stock exchange. The argument was that if investors had access to the tax return data, analysts might have detected the fraudulent books before the company went down. Canellos and Kleinbard have argued that this would not work: what would be more useful for both tax auditors and investors would be to have access to a public book-tax reconciliation schedule which would "provide a useful platform for highlighting transactions which are likely to involve manipulation for tax and accounting concepts" (Canellos & Kleinbard, 2002, p. 2). Theodore Sims (2002) suggested that making corporate returns available in a useful form on a website would enable a system of rewards for private auditors (bounty hunters) who brought new tax shelters to light. To motivate private auditors to pick over corporate tax returns in search of shelters, Sims suggests a bounty of say 20 cents in every dollar recovered by the tax authority payable by the taxpayer to the private auditor on top of any other tax penalty. "The most effective way of channelling sufficient resources into prevention is to make it as profitable to police corporate shelters as it has obviously become to purvey them" (Sims, 2002, p.736).⁴

The idea is an old one that can be applied to all domains of regulation (Crumplar, 1975). During the fourteenth and fifteenth century when the English state was weak in its enforcement capability, *qui tam* suits were relied upon heavily.⁵ An offender against laws subject to *qui tam* could be compelled to pay half the penalty incurred to an informer. Abuses of private prosecutions became so rife that *qui tam* fell into disrepute and disuse. Five centuries later in the United States Senator Grassley sponsored 1986 revisions to the False Claims Act that put *qui tam* on a more principled footing (Grassley 1998; Department of Justice 2003). Since then, over US\$12 billion, \$2.1 billion in 2003, has been recovered in *qui tam* actions concerning false claims to the US government, mostly for defrauding federal health programs or the defence budget (Department of Justice, 2003; <http://www.falseclaimsactatpaceandrose.com>). This historically recent American *qui tam* has proved less rife with abuse than its English precursor because the whistle blower against say a defence contractor who is fraudulently extracting payments from the Pentagon must first give the Department of Justice a chance to take over the action. If Justice wins, the whistle blower gets 15 to 25 percent of any settlement or judgement attributable to the fraud identified by the whistle blower. Justice decides to take on most of the meritorious False Claims Act actions because if the case is meritorious and Justice declines to take it over, the whistle blower's legal team can still take a private action and win 30 percent of the penalty, leaving the revenue poorer and the Justice Department

embarrassed by an error of judgment. On the other hand, legal counsel for a whistle blower with an unmeritorious case will counsel caution once the Department of Justice declines to take over the prosecution. Most whistle blowers who launch *qui tam* actions are middle managers or senior management from the corporation complained against. Hence, just as Slaughter's trans-governmental networks disaggregated states, *qui tam* disaggregates corporations, turning one part of a corporation (the whistle blower cum bounty hunter) against lawbreaking parts of the same organization.

Qui tam in effect networks whistle blowers with law firms, state regulators and prosecutors, extending the intelligence, evidence-gathering and litigation capabilities of the state in big, difficult cases. The reason *qui tam* was invented in fourteenth century England was to compensate for weakness in state regulatory capacity. The 1863 False Claims Act was first introduced by a Lincoln administration in the US that had little federal prosecutorial capacity to go after fraudulent over-billing of the Union Army. Across the globe today it still might be true that where state capacity is weakest the case for reliance on *qui tam* is strongest. Obversely, where state regulatory capacity is strong, private prosecution to fill gaps left gaping by failed public enforcement is less critical. In this sense, *qui tam* in the US should be a least likely case of *qui tam* adding value (Eckstein, 1975). The fact that it clearly has added value there in the context of False Claims Act enforcement (Department of Justice, 2003; Grassley, 1998) should give hope that *qui tam* might prove valuable in weak states where opportunities for bounty hunting are more plentiful.

On the other hand if the court system and justice bureaucracy themselves in a developing country are so inefficient or corrupt that they cannot cope with surges of *qui tam* actions, then these greater opportunities may simply not be practically available to be seized. Even in such circumstances, a strategy that can rely on private resources to do much of the justice bureaucracy's work for it has more prospects than reliance on a wholly public process. The new Grassley proposals on making corporate tax returns more effectively public on the internet so that a private tax auditing industry might emerge need not depend on courts. It could work by practitioners in this new private market in tax virtue taking the finding of their private analysis to the public tax authority. If the tax authority administratively assesses an extra \$10 million dollars in tax that the corporation voluntarily pays or settles (which is what normally happens) then the private tax auditor might win her \$2 million *qui tam* payout without going near a courthouse. Note also how the private auditor can help make responsive regulation work by being a check on corrupt tax officers, prosecutors and other officials (see Ayres & Braithwaite, 1992, ch.3). When the corrupt official reaches a cosy settlement with the corporation that fails to collect the tax owed, the private auditor has an interest in exposing this to his administrative and political masters who have an interest in higher tax collections, and to the courts if necessary, in order to collect the full bounty owed to the private auditor.

Enforcement of labour standards is another area where *qui tam* has been advocated (Braithwaite, 2005c). Private prosecutions by trade unions for underpayment of wages, where the union could collect 30 per cent of the penalty imposed on the company, would mostly work by threatening the private prosecution in order to trigger

settlement negotiations, while rarely in practice having to rely on an overburdened court system.

Networking with lawyers who specialize in *qui tam* actions against multinational companies would be networking with lawyers who in some cases could mount actions in foreign courts against multinationals – thereby obviating the need to rely on courts in the poor country. While it is unimaginable that False Claims statutes to compensate developing states could be enforced in Western courts, in tort cases like the Bhopal chemical pollution disaster in India and the litigation against BHP⁶ by Papua New Guinea villagers over the destroying of their livelihoods by the pollution of the Fly River, globally networked law firms have had major impacts on multinationals.

6. Conclusion

We have argued that developing economies are more lacking in all the capacities necessary to make responsive regulation work well than are wealthy societies. In attempting to lay a foundation for policy ideas to compensate for this, the essay overgeneralises these deficits. Some larger developing societies such as India have strong democratic states with substantial, sophisticated bureaucracies and courts. Many “failed states” such as Afghanistan are strong societies with formidable regulatory capacities in civil society through institutions such as *jirga* (Wardak, 2004).

Whatever the level of these deficits, in an era of networked governance, weaker actors can enrol stronger ones to their projects if they are clever. Anne-Marie Slaughter’s work suggests that the globe is strewn with disaggregated bits of strong states that might be enrolled by weak ones (and by weak NGOs)(Slaughter, 2004). The developing country civil aviation regulator can enrol the US Federal Aviation Administration to stand up to an airline that flouts safety standards in the developing country; the developing country health regulator can enrol the Food and Drug Administration to audit the unsafe clinical trials on a new drug being conducted on its people. Developing country NGOs may be weak, but are becoming stronger both in their own right and in their capacity to enrol Northern NGOs and international regulatory organizations into projects to compensate for the weak regulatory capacities of developing states. Responsive escalation up a regulatory pyramid can hence be accomplished not only by escalating state intervention, but also as Peter Drahos (2004) suggested, by escalating the networking of new tentacles of domestic and transnational governance. The core idea of responsive regulation as a strategy actually has special salience for resource-poor states. This is the idea that no regulator has the resources to consistently enforce the law across the board and therefore limited enforcement resources need to be focussed at the peak of an enforcement pyramid. Networking escalation is an interesting elaboration of how to make the most of limited regulatory capacity.

Finally, we have seen that mobilizing public virtue to regulate private vice is not the only path around capacity deficits. Private markets in virtue can also be mobilized to regulate vice, indeed to flip markets in vice to markets in virtue (Braithwaite, 2005a). One example is enabling bounty hunting by privatised tax auditors through making

crucial information on corporate tax returns public on the Internet. Another is the kind of *qui tam* actions under the False Claims Act that have significantly cleaned up the US defence contracting industry since 1986. Where state capacity is weakest, both *qui tam* and responsive escalation via networking with progressively more private and public enforcers should pay the highest dividends. Moreover, networking regulatory partnerships also structurally reduces the benefits of capture and corruption in those developing economies that are endemically prone to corruption. Responsive regulation is a worrying strategy in corrupt societies because it puts more discretion in the hands of regulatory bureaucrats who can use that discretion to increase the returns to corruption. Both the strategies of networking around state incapacity and mobilizing private markets for enforcing virtue have the attractive feature of exposing and preventing regulatory corruption.

Endnotes

¹ On the history of the legal profession as a regulatory partner of the US state, see Halliday (1987).

² Obviously I am uncomfortable about the concept of the post-regulatory state because I think that for most of human history a large part of the regulation that matters most has not been undertaken by states.

³ Rod Rhodes made the following insightful comment on a earlier draft of this paper: “I worry policy networks are a form of political oligopoly. They privilege some interests and specifically exclude others. Moreover, they colonise specific policy arenas. So there is no competition/regulation within either a network or an arena, only between networks, and that is restricted because their interests are often too confined to one arena and do not span them.” I am indebted to Rod Rhodes for stimulating the reflections in this paragraph.

⁴ On the effectiveness of private bounties for detecting corporate wrongdoing generally, see Fisse and Braithwaite (1983), 251-254, 283.

⁵ The Latin “qui tam pro domino rege, quam pro se ipso in hac parte sequitur” translates as “who as well for the king as for himself sues in this matter”

⁶ Now BHP Billiton

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