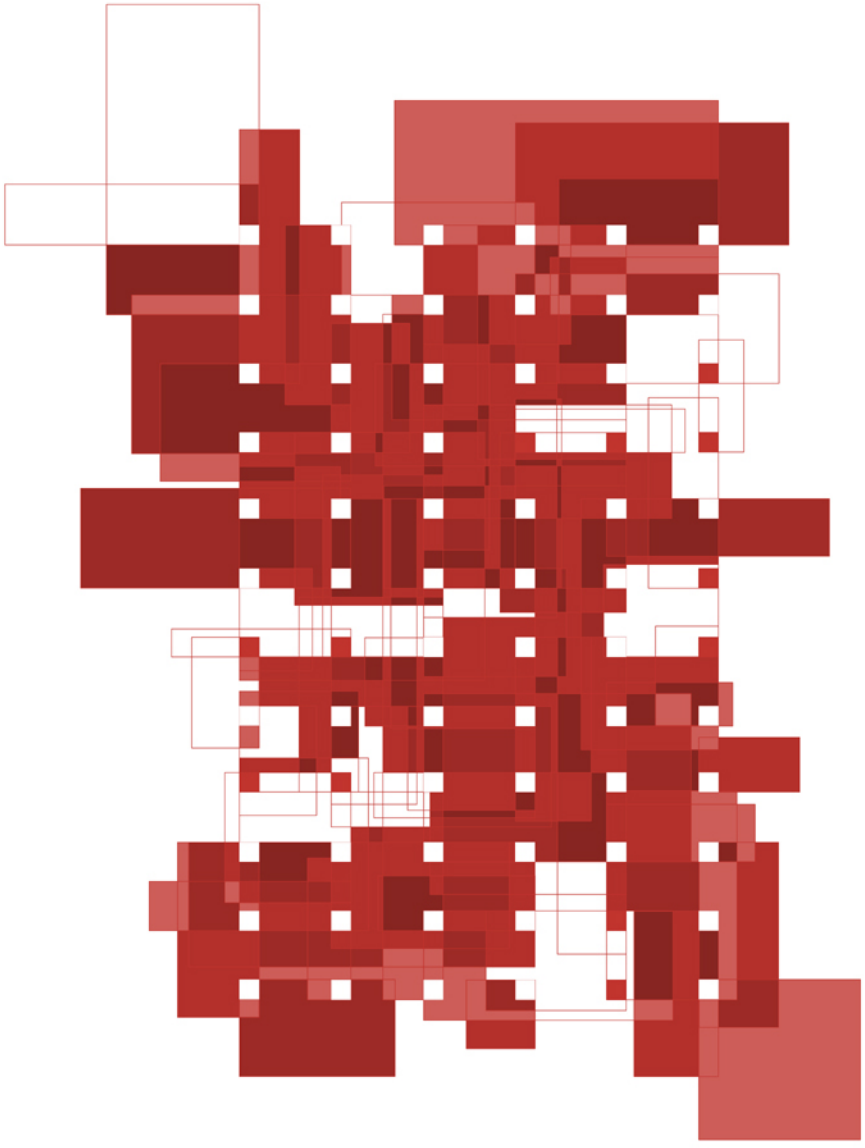
ESPECIAL

ECONOMIC AND SOCIAL REGULATION, ACCOUNTABILITY AND DEMOCRACY

NOVEMBRO 2005
ISSN 1808-2432

Revista DIREITO GV



FUNDAÇÃO GETULIO VARGAS

DIREITO GV
ESCOLA DE DIREITO DE SÃO PAULO DA FUNDAÇÃO GETULIO VARGAS

Revista DIREITO GV

ISSN 1808-2432

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ESPECIAL 1 NOVEMBRO 2005

FUNDAÇÃO GETULIO VARGAS

DIREITO GV

ESCOLA DE DIREITO DE SÃO PAULO DA FUNDAÇÃO GETULIO VARGAS

ISSN 1808-2432

NOVEMBRO 2005
SÃO PAULO - SP

PUBLICAÇÃO SEMESTRAL DA
FUNDAÇÃO GETÚLIO VARGAS
ESCOLA DE DIREITO DE SÃO PAULO
(DIREITO GV)

TIRAGEM 1.000 EXEMPLARES

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ED. FUNDAÇÃO GETÚLIO VARGAS
ISSN 1808-2432

REVISTA DA ESCOLA DE DIREITO DE SÃO PAULO
(DIREITO GV) DA FUNDAÇÃO GETÚLIO VARGAS

EDITORES
NOVEMBRO 2005, JOSÉ RODRIGO RODRIGUEZ
INCLUI BIBLIOGRAFIA

1. DIREITO – PERIÓDICOS. I. SÃO PAULO (CIDADE). DIREITO GV

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PRODUÇÃO INDUSTRIAL
IMPRESSÃO E ACABAMENTO: GRÁFICA BANDEIRANTES
DATA DE IMPRESSÃO: NOVEMBRO 2005
TIRAGEM: 1000 EXEMPLARES

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ESPECIAL 1 NOVEMBRO 2005

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INTRODUÇÃO

REGULAÇÃO ECONÔMICA E SOCIAL, ACCOUNTABILITY E DEMOCRACIA: CONTEXTO E PERSPECTIVAS DO DEBATE

Paulo Todescan Lessa Mattos [1]

A Constituição de 1988 é um reflexo da crise de legitimidade que marcou o processo de redemocratização no Brasil após duas décadas de regime autoritário. A partir do novo marco constitucional e das eleições diretas em 1989, assistimos um amplo processo de reforma do Estado na década de 90. Ao longo desse processo é possível identificar a ampliação dos movimentos sociais e da organização de atores antes à margem do processo político. Às garantias de direitos de associação, de livre acesso à informação e de participação previstas na Constituição somam-se novos mecanismos institucionalizados de participação pública nos processos decisórios sobre a formulação de políticas públicas e novas formas de controle democrático da ação regulatória do Estado.

Nesse contexto, as relações entre o Poder Executivo e os outros dois poderes (Legislativo e Judiciário) começou a se reconfigurar. Ao mesmo tempo, as relações entre Estado e sociedade civil também. Temas relevantes em matéria de formulação de políticas públicas passam a estar na pauta do dia da imprensa e dos meios de comunicação de massa. Novos canais de circulação de poder político foram constituídos.

O modelo de agências reguladoras autônomas adotado no Brasil no contexto da reforma do Estado na década de 90 insere-se nesse cenário. Tal modelo teria estabelecido uma nova dinâmica política para a ação regulatória do Estado. A formulação de políticas setoriais que antes estava restrita aos gabinetes ministeriais, aos conselhos institucionalizados no interior da burocracia estatal da Administração Direta, subordinada às decisões políticas do presidente da República e ao jogo de barganhas políticas com o Congresso, passou a ser formulada de forma insulada por técnicos especializados, porém relativamente aberta ao público afetado pelas normas editadas pelas agências.

Dessa forma, as agências reguladoras se transformaram em um novo lócus de circulação de poder político, redefinindo as relações internas ao Poder Executivo na regulação de setores da economia brasileira e as condições de barganha política entre este Poder e o Poder Legislativo. Ao mesmo tempo, as agências se transformaram em uma nova arena política de participação de atores da sociedade civil na eleboração de políticas públicas.

Esse novo cenário na ação regulatória do Estado permitiria afirmar que, a partir das reformas da década de 90, um novo modelo Estado regulador começa a se delinear no Brasil. Este novo modelo de ação regulatória do Estado teria características muito distintas do modelo anterior.

No contexto de redemocratização do Brasil e de valorização da sociedade civil e da esfera pública como elementos constitutivos da democracia e, assim, das condições de legitimidade de políticas públicas, as agências reguladoras surgem como uma possibilidade de descentralização da ação regulatória do Estado e de nova arena decisória em matéria de políticas públicas, não limitada, porém conectada, ao processo de barganha político-eleitoral característico do eixo de circulação de poder político (Administração Direta - Poder Legislativo).

O modelo de agências reguladoras introduziu novos mecanismos de ***controle democrático*** (*accountability*)[2] da atuação do Estado na regulação de setores da economia brasileira. Os principais mecanismos são as consultas públicas e as audiências públicas, que são realizadas

antes da edição de normas pela agência na regulação do setor.

Tais mecanismos poderiam ser qualificados como mecanismos de participação pública ou de deliberação pública em processos decisórios sobre a formulação do conteúdo da regulação. Porém, existe uma série de limitações procedimentais e institucionais que podem ser identificadas e avaliadas na caracterização e análise do funcionamento das consultas públicas e das audiências públicas.

Dentro da lógica do novo modelo de Estado regulador no Brasil, o uso desses mecanismos nas agências reguladoras teria por justificativa tornar a atuação desses órgãos mais controlada pelo público (cidadãos afetados pela regulação setorial). Nesse sentido, os mecanismos de consultas públicas e audiências públicas adotados no interior das novas agências reguladoras podem ser tomados como a garantia de legitimidade do conteúdo da regulação, uma vez que, por meio destes, estariam sendo expressos e supostamente atendidos os interesses do público (i.e. grupos de interesse) afetado pelas políticas definidas pela agência.

No plano jurídico-formal, a fonte de legitimidade da ação regulatória do Estado continua sendo a lei setorial aprovada pelo Congresso. No entanto, no plano político a fonte de legitimidade democrática das políticas formuladas pelas agências reguladoras deixariam de ser apenas os interesses e as decisões do presidente da República (eleito) e dos congressistas (eleitos).

No novo modelo de agências reguladoras adotado no Brasil, nem o presidente e nem o Congresso podem rever as decisões do órgão regulador dotado de autonomia decisória. A única revisão possível é a judicial. Assim sendo, o processo decisório sobre o conteúdo da regulação setorial formulado pelas agências autônomas passou a ter como garantia de seu controle democrático, para além da revisão judicial (possível, porém limitada), essencialmente os mecanismos de consultas públicas e audiências públicas introduzidos no novo modelo. Haveria, portanto, deficits de legitimidade e, ao mesmo tempo, novos desafios no controle democrático dos processos decisórios internos às agências.

Nesse contexto, é possível afirmar que a adoção de mecanismos de consultas públicas e de audiências públicas pode significar um avanço em termos de *accountability* do processo decisório sobre políticas setoriais no Brasil. Isso ocorreria na medida em que a "caixa-preta" dos ministérios perde relevância no processo decisório, permitindo que outros grupos de interesse, que não apenas aqueles com acesso privilegiado aos canais de circulação de poder político na relação presidente-Congresso, participem do processo decisório e tenham os seus interesses ouvidos no interior das novas agências.

A adoção de tais mecanismos teria um "potencial democrático", apesar da diminuição do espaço dos mecanismos tradicionais de controle político pela via eleitoral *(accountability vertical)*, uma vez que os conselheiros que compõem as agências reguladoras não são eleitos, ou na relação entre os órgãos que compõem os poderes Executivo e Legislativo *(accountability horizontal)*.

Diante desse quadro, o Direito ganha uma nova dimensão no debate sobre a legitimidade da ação regulatória do Estado. Avaliar as condições decisórias sobre a formulação de políticas públicas pode ser um tarefa realizada a partir do Direito e não apenas da Ciência Política. Porém, para isso, faz-se necessário trabalhar com um modelo de análise que dê conta da complexidade das relações sociais próprias do fenômeno do Estado regulador.

Tal modelo precisa permitir uma análise que seja capaz de avaliar o desenho institucional de órgãos reguladores e sua relação com o Poder Executivo (Administração Direta), com o Poder Legislativo e com o Poder Judiciário

para além de uma concepção liberal de democracia que assume uma relação estática entre tais poderes. Ao mesmo tempo, deve ser um modelo capaz de avaliar os procedimentos institucionalizados para tomada de decisão, assumindo tais procedimentos como meios de controle democrático e de deliberação pública sobre questões relevantes de ordem política que estão na base da escolha de técnicas administrativas para regular a economia e a vida social – a definição do conteúdo da regulação.

E a definição do conteúdo da regulação determina as condições materiais de distribuição de recursos e condiciona o exercício de direitos por parte dos atores afetados pela regulação. Em outras palavras, as escolhas feitas na formulação da regulação de mercados determina, em síntese, as condições de desenvolvimento econômico e social.

Daí a importância de se avaliar as condições de controle democrático dos processos decisórios internos à burocracia estatal (i.e. o desenho institucional dos órgãos reguladores e do processo administrativo, bem como a dinâmica política da tomada de decisões).

Por fim, tem que ser um modelo capaz de avaliar as condições de participação na esfera pública brasileira. Saber quem é o público (i.e. grupos de interesse) que está atuando junto às agências, influenciando o conteúdo da regulação, e como está se dando o processo decisório no interior das agências passou a ser importante para uma análise das condições de legitimidade democrática da formulação de políticas setoriais no Brasil pós-reforma do Estado.

Os modelos de análise predominantes na doutrina jurídica brasileira em matéria de direito administrativo e direito econômico não são, ao meu ver, suficientes para compreender a complexidade do funcionamento do Estado regulador e, principalmente, as condições de legitimidade de processos decisórios sobre a formulação de políticas públicas num contexto de delegação legislativa (ou de exercício de *capacidade normativa de conjuntura)* por órgãos reguladores dotados de autonomia decisória. Seriam modelos ainda presos a uma concepção de direito liberal, focados em análises de adequação lógico-formal de normas a um ordenamento jurídico hierarquicamente constituído.

Por outro lado, modelos da análise formulados no debate teórico político-social brasileiro acabam também sendo insuficientes, pois tendem a ter um concepção restrita de democracia e de *accountability*. Ou estão presos a modelos de democracia liberal – fundados na compreensão das relações sociais a partir do individualismo metodológico centrado em noção de racionalidade puramente instrumental – ou estão voltados para um ideal republicano de democracia excessivamente idealizado – que exige um grau elevado de cidadania e de dinâmica da esfera pública por vezes incompatível com as condições reais de organização da sociedade civil.

Nesses modelos, a *accountability* é pensada, por um lado, como controle de resultados da administração (em termos de eficiência dos resultados), centrada no processo eleitoral *(accountability vertical)* como forma de responsabilização ou numa relação de pesos e contrapesos entre os três poderes entendida de forma por demais mecânica ou estática. Por outro lado, começa a ser pensada de forma a incluir a dinâmica de atuação de grupos de interesse que se formam na sociedade civil, mas, dados os traços de um republicanismo idealizado, não consegue dar conta de problemas substantivos de legitimidade democrática.

Esse conjunto de questões motivou um grupo de jovens pesquisadores ligados ao Núcleo Direito e Democracia do CEBRAP, no contexto de projeto temático FAPESP coordenado pelos professores Ricardo Terra (Filosofia USP) e Marcos Nobre (Filosofia UNICAMP), a estudarem o fenômeno da reforma do Estado no Brasil e a mudança nas técnicas administrativas na regulação econômica e social.

O evento *Economic and Social Regulation, Accountability and Democracy* foi organizado por membros do Núcleo Direito e Democracia do CEBRAP - Mariana Mota Prado, Jean Paul Rocha, Rafael Oliva, Diogo Coutinho, Tiago Cortez, Paulo Todescan L. Mattos - e por pesquisador que à época concluia o seu doutorado na Yale Law School - Caio Mario da Silva Pereira Neto.

O entusiasmo desse grupo naquele momento foi fundamental para que fosse possível juntar em dois dias de debates intensos acadêmicos representantes de diversas correntes de pensamento jurídico, político-social, filosófico e econômcio no debate norte-americano, europeu e brasileiro.

Além das teses de doutorado sobre o tema dos integrantes desse grupo concluídas nos últimos dois anos ou em fase final de elabroação, o mesmo grupo organizou coletânea de traduções de textos clássicos sobre regulação econômica e direito administrativo publicada pela *Editora 34* na data da conferência, entitulada *Regulação Econômica e Democracia: o debate norte-americano*[3]. Outra coletânea com traduções de textos de referência no debate europeu sobre o tema está pronta e será publicada em breve pela *Malheiros Editora*.

A realização da conferência foi um reflexo da produção acadêmica desse grupo e, principalmente, resultado de quatro anos de intensos debates no Núcleo Direito e Democracia do CEBRAP, coordenado pelos professores Ricardo Terra e Marcos Nobre - os principais motivadores da transformação da produção acadêmica jurídica da minha geração.

Também foi essencial para a realização do evento o apoio recebido pela Yale Law School, pela Fundação de Amparo à Pesquisa do Estado de São Paulo e pela Escola de Direito de São Paulo da Fundação Getulio Vargas.[4]

Os professores Ary Oswaldo Mattos Filho e Antonio Angarita generosamente abriram as portas da Fundação Getulio Vargas para esse grupo de jovens pesquisadores no campo do Direito.

Os resultados da conferência *Economic and Social Regulation, Accountability and Democracy* foram, além dos intensos debates que marcaram as pesquisas que o grupo vinha realizando à época, a produção de 11 papers inéditos por acadêmicos de instituições de ensino e pesquisa de ponta no Brasil, nos Estados Unidos e na Europa. Além dos papers inéditos, o professor Bruce Ackerman, um dos principais constitucionalistas norte-americanos, trouxe ao debate o artigo *The New Separation of Powers,* trabalho provocante que já havia sido publicado na *Harvard Law Review*.[5]

Agora, com a criação da revista da Escola de Direito de São Paulo da Fundação Getulio Vargas, abriu-se uma excelente oportunidade para publicação dos *papers* inéditos que foram especialmente elaborados para a conferência.[6] Os trabalhos estão publicados na integra, tal como foram submetidos ao público durante o debate. O fato de estarem na língua inglesa decorre de terem sido elaborados para uma conferência internacional.

A sua publicação na Revista da FGV Direito permitirá não só o acesso de estudantes e pesquisadores ao debate sobre os temas e questões discutidos na época, bem como o início de novas pesquisas inovadoras em Direito e a continuação do trabalho que procuramos inciar no Núcleo Direito e Democracia do CEBRAP.[7]

Segue breve descrição dos textos, na sequência em que foram apresentados e debatidos durante o evento, conforme programação reproduzida abaixo.

Fernando Limongi

Institutions, Presidents and Agencies

O autor faz revisão e crítica dos estudos e métodos de análise sobre o funcionamento comparado de instituições políticas. Em particular, o debate neo-institucionalista norte-

americano não seria suficiente para explicar as especificidades do processo legislativo brasileiro, bem como a relação entre Poder Executivo e burocracia estatal. Nesse ponto, o autor estabelece diálogo crítico com o trabalho de Bruce Ackerman, *The New Separation of Powers*, o qual acabaria por generalizar o diagnóstico do funcionamento de sistemas políticos, a partir do diagnóstico marcado por modelo de análise específico sobre o funcionamento do sistema político norte-americano.

Leonardo Avritzer

New Public Spheres in Brazil: Local Democracy and Deliberative Politics

O autor apresenta as características do processo de ampliação de experiências participativas no processo decisório em matéria de políticas públicas no Brasil. O foco do trabalho, do ponto de vista empírico, está nas experiências sobre orçamento participativo. A partir a análise das experiências empíricas, o autor procura discutir os ganhos e déficits democráticos decorrente da participação dos atores afetados pelo conteúdo das políticas objeto de deliberação pública. Por fim, o autor procura destacar as especificidades da dinâmica da esfera pública do Brasil, apresentando problemas decorrentes de diferentes formas de participação pelo público, o que coloca em foca a tensão entre participação e deliberação (ou entre as formas de mensuração dos ganhos democráticos decorrentes da mera participação sem fala ou da participação com deliberação).

Charles Sabel

O autor, mais do que um *paper* conclusivo, elaborou uma agenda de pesquisa sobre a dinâmica do funcionamento de esferas públicas e sua relação com o processo decisório em matéria de políticas públicas. Na agenda de pesquisa proposta, o autor provoca o debate sobre os limites da compreensão do processo democrático de produção de normas limitado ao funcionamento do Poder Legislativo e da Administração, tal como entendido pelos modelos teóricos que procuraram interpretar a reforma do Estado norte-americana marcada pelo *New Deal* ou a reforma do Estado européia caracterizada pela criação das instituições que formaram a esfera administrativa da União Européia. Ao mesmo tempo, o autor procura destacar as especificidades da dinâmica das reformas do Estado latino-americana, do funcionamento da Administração e da esfera pública de país como o Brasil (ao estabelecer ponte com o trabalho de Leonardo Avritzer), em contraposição aos casos norte-americano e europeu.

Julia Black

Proceduralisation and Polycentric Regulation

A autora discute em seu artigo, a partir de diálogo com a literatura acadêmica européia e norte-americana sobre democracia deliberativa, as dificuldades decorrentes da introdução da procedimentos deliberativos para a tomada de decisões na definição do conteúdo da regulação. Em especial, a autora destaca os problemas decorrentes da tensão entre diferentes racionalidades comunicativas e, portanto, de compreensão pelo público de aspectos técnicos do conteúdo da regulação. Assumindo as exigências decorrentes do modelo de democracia deliberativa, a autora procura discutir mecanismos procedimentais de tradução e de resolução de disputas envolvendo problemas técnicos, os quais responderiam aos desafios decorrentes da introdução de procedimentos deliberativos na formulação de normas técnicas.

Fábio W. Reis

Deliberation, Interests and Pluralism

O autor realiza crítica teórica aos pressupostos do modelo de democracia deliberativa habermasiano, enfatizando tensão entre ação comunicativa cuja racionalidade visa o entendimento a partir da livre argumentação e a racionalidade

instrumental que seria própria do processo de definição de normas técnicas na prática do funcionamento das instituições. Ainda no plano teórico, o autor destaca os problemas de legitimidade e eficácia (entendida como eficiência) das normas técnicas, procurando demonstrar os limites do modelo de democracia deliberativa para a compreensão da definição do conteúdo da regulação, diante da ausência de situação comunicativa ideal com vistas apenas ao entendimento.

Jerry L. Mashaw

Judicial Review of Administrative Action: Reflections on Balancing Political, Managerial and Legal Accountability:

O autor enfoca a questão da revisão judicial de decisões administrativas, estabelecendo análise do papel da revisão judicial enquanto mecanismo de controle democrático da Administração (para além do papel do Legislativo) e de proteção dos direitos dos cidadãos afetados pelo conteúdo da regulação. Além disso, o autor procura discutir os problemas inerentes à revisão judicial no contexto da regulação, especialmente por não ser, de um lado, organismo composto do membros eleitos e, de outro lado, por não ser dotado de conhecimento técnico especializado tal como os órgãos reguladores da Administração. Diante da exigência de controle judicial e dos problemas decorrentes desse tipo de controle, o autor procura estabelecer reflexão sobre as condições e limites do controle judicial de decisões administrativas.

José Reinaldo de Lima Lopes

The Traditional Dialogue Between Law & Economics

O autor estabelece discussão no plano teórico sobre a tensão existente entre racionalidade jurídica e racionalidade econômica. Os limites e condições da introdução da racionalidade econômica no processo de motivação do conteúdo da regulação são discutidos. Ao mesmo tempo, o autor destaca, reconstruindo exemplos na história do funcionamento das instituições, a especificidade e a autonomia do sistema jurídico, com sua racionalidade própria de funcionamento, apesar da relação existente com o sistema econômico. Por fim, o autor propõe agenda de pesquisa sobre os conflitos entre o processo decisório sobre o conteúdo da regulação interno às agências reguladoras e a revisão judicial de decisões administrativas.

Marcus André Melo

Institutional design, normative political theory and accountability

O autor discute o funcionamento das instituições políticas e o seu controle democrático pelos cidadãos, enfocando, especialmente, o processo eleitoral com o mecanismo clássico das democracias modernas de massa de veto ou sanção do político eleito após cumprido o seu mandato. No caso da criação de instituições que se afastam da dinâmica dos processos eleitorais - como é o caso das agências reguladoras dotadas de autonomia decisória - o controle democrático das decisões administrativas se torna complexo. O autor procura analisar, no plano teórico, as condições de controle democrático - accountability - de instituições políticas, considerando o desenho institucional em questão e sua posição na articulação na relação com cidadãos-eleitores.

Susan Rose-Ackerman

The Challenge of Poor Governance and Corruption

A autora discute mecanismos de governança no funcionamento de instituições - incluindo órgãos reguladores - que podem limitar os incentivos à corrupção. Dessa forma, o problema da corrupção é enfocado com destaque para os problemas relacionados ao funcionamento da Administração. Os riscos da corrupção e do mau funcionamento de órgãos administrativos estariam ligados a fatores diversos,

sendo que o controle da Administração e da regulação de mercados, principalmente na forma de prestação de contas com justificativa para as medidas adotadas, pode ajudar a reduzir os fatores que levam à corrupção. A autora apresenta exemplos de programas e mecanismos de governança que podem ser adotados no combate à corrupção e melhora do funcionamento de órgãos administrativos.

Edmund Amann and Werner Baer

From the developmental to the regulatory state: the transformation of the government's impact on the Brazilian economy

Os autores apresentam análise da passagem do modelo de Estado desenvolvimentista que marcou o cenário econômico brasileiro dos anos 30 aos anos 80 para modelo de Estado regulador marcado pelas reformas do Estado nos anos 90. O novo papel do Estado como agente regulador é discutido criticamente a partir de exemplos das políticas de privatização e regulação dos setores de energia elétrica e telecomunicações no Brasil. Por fim, os autores discutem os desafios da tentativa de retomada de políticas desenvolvimentistas - em parte delineadas no início do Governo Lula - diante da dinâmica da regulação de mercados e dos instrumentos regulatórios disponíveis após as reformas dos anos 90.

Luciano Coutinho

Regulation and Development: Reflections in the aftermath of Neoliberalism

O autor discute os limites dos pressupostos do modelo neoliberal de atuação do Estado que marcou as reformas nos anos 90, combinando privatização com estimulo à concorrência como um fim em si mesmo. O autor estabelece análise crítica da regulação concorrencial de mercados, considerando as especificidades estruturais de cada mercado. Especialmente nos casos dos mercados caracterizados por grandes economias de escala, como é o caso de serviços de infra-estrutura e serviços públicos, ou, principalmente, mercados com características de monopólio natural, a combinação privatização-concorrência-regulação não seria adequada ou suficiente para o desenvolvimento econômico setorial.

Segue abaixo o programa do evento, para que o leitor possa comprender em que contexto cada um desses *papers* foi discutido e quais foram os moderadores que participaram do evento para estabelecer contrapontos entre os textos e os debates com o público presente durante a conferência

Economic and Social Regulation, Accountability and Democracy

The Conference on Economic and Social Regulation, Accountability and Democracy took place at Escola de Direito de São Paulo da Fundação Getulio Vargas (FGV Direito). It was organized by Centro Brasileiro de Análise e Planejamento (CEBRAP), Núcleo Direito e Democracia, with support o Yale Law School, FGV Direito and Fundação de Amparo à Pesquisa do Estado de São Paulo (FAPESP)

Its purposes was to promote a debate over the changes, problems and possibilities brought about by the recent implementation of regulatory agencies and structures in Brazil. For that purpose, invited panelists from Brazil, United States and England presented and discussed empirical as well as theoretical scholarship related to these matters.

The Conference was organized in six panels devoted to different aspects of the regulatory reform. Discussions in each panel were based on papers prepared by two panelists over a common issue. The conference tried to promote debate between the panelists as well as to create an opportunity of dialogue between the panelists and all other participants.

Program Agenda and Speakers

• March 15, 2004

Independent Regulatory Agencies: Separation of Powers and Legitimacy

Moderator

José Arthur Giannotti (Emeritus Professor of Philosophy at University of São Paulo - USP / Former President of Brazilian Center of Analysis and Planning - CEBRAP)

Panelists

Fernando Limongi (Professor of Political Science at University of São Paulo - USP / President of Brazilian Center of Analysis and Planning - CEBRAP)

Bruce Ackerman (Sterling Professor of Law and Political Science at Yale University)

Regulatory State and Deliberative Democracy

Moderator

Marcos Nobre (Professor of Philosophy at University of Campinas / CEBRAP Law and Democracy Nucleus Director)

Panelists

Leonardo Avritzer (Professor of Political Science at Federal University of Minas Gerais - UFMG)

Charles Sabel (Maurice T. Moore Professor of Law and Political Science at Columbia University)

Proceduralizing Regulation

Moderator

Paulo Mattos (Researcher at Brazilian Center of Analysis and Planning)

Panelists

Julia Black (Reader in Law at London School of Economics and Political Science)

Fábio Wanderley Reis (Professor of Political Science at Federal University of Minas Gerais - UFMG)

• March 16, 2004

Regulatory Agencies, Judicial Review, and Democracy

Moderator

Carlos Ari Sundfeld (Professor of Law at Catolica University of São Paulo)

Panelists

Jerry Mashaw (Sterling Professor of Law at Yale University

José Reinaldo Lima Lopes (Professor of Law at University of São Paulo)

Institutional Design, Corruption and Accountability

Moderator

Denilson Werle (Researcher at Brazilian Center of Analysis and Planning)

Panelists

Marcus André Melo (Professor of Political Science at Pernambuco Federal University)

Susan Rose-Ackerman (Henry R. Luce Professor of Jurisprudence, Law School and Political Science at Yale University)

Regulation and Economic and Social Development

Moderator

Calixto Salomão Filho (Professor of Law at University of São Paulo - USP)

Panelists

Edmund Amann (Professor of Economics, School of Economics, University of Manchester, UK)

Luciano Coutinho (Professor of Economics at University of Campinas - UNICAMP)

NOTES

1 Doutor em filosofia e teoria geral do direito pela USP, integrante do Núcleo Direito e Democracia do Centro Brasileiro de Análise e Planejamento (CEBRAP), professor do Programa de Especialização em Direito da Fundação Getulio Vargas (FGVSP).

2 O termo accountability, em inglês, tem sido traduzido para o português como responsabilização, prestação de contas ou, ainda, responsabilização com prestação de contas. Contudo, o uso desse termo na literatura de língua inglesa no campo das ciências sociais me parece mais amplo. Não é incomum nessa literatura o uso do termo accountability para qualificar formas de controle democrático de instituições políticas.

3 Paulo Todescan Lessa Mattos (coord, et alli). Regulação Econômico e Democracia: o debate norte-americano, São Paulo: Editora 34, 2004.

4 Cabe mencionar também o apoio do Consulado Norte-Americano em São Paulo, sem o qual a conferência não teria sido possível.

5 Bruce Ackerman, "The New Separation of Powers" in Harvard Law Review, volume 113, January 2000, number 3.

6 Com a exceção, portanto, do texto "The New Separation of Powers".

7 Esse evento foi o segundo evento organizado por pesquisadores do Núcleo Direito e Democracia do CEBRAP em parceria com a Escola de Direito de São Paulo da Fundação Getulio Vargas. O primeiro foi o evento "O que é pesquisa em Direito?, realizado no final de 2002, cuja transcrição dos debates foi publicada pela Editora Quartier Latin no final de 2004. Com a presente publicação, os resultados de ambos os eventos se tornaram mais acessíveis ao publico. Agradeço mais uma vez ao José Rodrigo Rodriguez, atual coordenador de pesquisa e publicações da Escola de Direito da FGV, por tornar essas publicações possíveis.

ECONOMIC AND SOCIAL REGULATION, ACCOUNTABILITY AND DEMOCRACY: CONTEXT AND PERSPECTIVES OF THE DEBATE

PAULO TODESCAN LESSA MATTOS[1]

The Constitution of 1988 reflects a crisis of legitimacy that characterized Brazil's redemocratization process after two decades of authoritarian regime. As of the new constitutional mark and the direct elections in 1989 we saw an extensive process of State reform throughout the 90's decade. In the course of this process it is possible to identify the expansion of social movements and the organization of participants, who in the past were kept aside of the political process. In addition to the guarantees of association rights, free access to information and participation provided for in the Constitution, there are new institutionalized mechanisms of public participation in decision-making processes with regard to the formulation of public policies and new ways of democratic control over the State's regulatory action.

In this context, the relations between the Executive Power and the other two Powers (Legislative and Judicial) began to reconfigure. As did the relations between the State and civil society at the same time. Relevant themes regarding the formulation of public policies enter the daily agenda of the press and mass communication media. New circulation channels were created for political power.

The model of autonomous regulatory agencies adopted in Brazil in the context of State reform in the 90's decade becomes part of this scenery. Which model would have established a new public policy dynamic for State regulatory action. The formulation of sectorial policies, previously confined to Minister cabinets and institutionalized councils within State's direct administration bureaucracy subject to presidential political decisions and political bargaining with the Congress, started being formulated by specialized technicians in independent manner, however, open to the public affected by norms issued by the agencies.

Thus, regulatory agencies became a new political power circulation locus redefining Executive Power internal relations as to regulation of sectors of the Brazilian economy and conditions for political bargaining between the Executive and Legislative Powers. At the same time, the agencies became a new political arena with civil society participants taking part in the preparation of public policies.

The State's new regulatory action scenery would allow one to say that since the 90's decade a new regulatory State model is being delineated in Brazil. The characteristics of the State's new regulatory action are significantly different from those of the previous model.

In the context of Brazil's redemocratization and favorable regard of the civil society and the public sphere as constitutive elements of democracy and accordingly, of the legitimacy of public policies, the regulatory agencies emerge as a new opportunity for decentralization of the State's regulatory action and as new decision-making arenas for public policies not limited to, but connected to, the political-electoral bargaining process that characterizes the circulating hub of political power (Direct Administration - Legislative Power).

The regulatory agencies model introduced new mechanisms for **democratic control** *(accountability)*[2] *of the State's performance relating to regulation of economic sectors of the Brazilian economy. The main mechanisms employed are public consultations and public hearings carried out prior to norms being issued by the relevant regulatory agency.*

The foregoing mechanisms could be defined as mechanisms of public participation or public deliberation within decision-making processes in connection with regulation content formulation. However, there remain a number of institutional and procedural limitations that can be identified and evaluated during the analysis and characterization of public consultation and public hearing functionings.

Consistent with the rationale of the new Brazilian regulatory state model the use of those mechanisms by regulatory agencies would be justified by the increased level of control exerted upon them by the public (citizens affected by sectorial regulation). In that sense, the mechanisms of public audiences and public hearings implemented within the new regulatory agencies could be seen as guarantees of regulation content legitimacy, since through them items of public interest (i.e. of interest to people affected by policies defined by the relevant agency) would be properly communicated and dealt with.

To a formal judicial level the source of legitimacy of the State's regulatory action would remain as the sectorial law approved by the Congress. However, at political level the source of democratic legitimacy of policies formulated by regulatory agencies would no longer be simply interests of and decisions made by the (elected) President and the (elected) members of the Congress.

In the new model of regulatory agencies implemented in Brazil, neither the President nor the Congress can review decisions made by an autonomous regulatory agency. The only possible review would be the judicial one. Therefore, the decision-making process on content of sectorial regulation formulated by autonomous agencies now has as guarantees of its democratic control, in addition to the judicial alternative (achievable, however, in limited manner) essentially the mechanisms of public consultations and public hearings introduced together with the new model. So, there would be deficits of legitimacy accompanied by new challenges for democratically controlling the agencies' internal decision-making processes.

In this context it is possible to assert that the adoption of mechanisms of public audiences and public hearings could mean an enhancement of accountability in the sectorial decision-making process in Brazil. This would occur as the 'black-boxes' of ministries gradually lose relevance in the decision-making process, allowing other interest groups, in addition to those already with privileged access to channels of political power circulation in the President-Congress relationship, to take part in the decision-making process and be heard in the new agencies.

The implementation of the foregoing mechanisms would have a 'democratic potential' notwithstanding a reduction in the space for traditional mechanisms of political control via elections (vertical accountability), since the council members that make up the Board of Directors of the Regulatory Agencies are not elected, or in the relationship (horizontal accountability) between organs that constitute the Executive and Legislative Powers.

In the abovementioned overall picture, Law gains a new dimension in the debate upon legitimacy of the State's regulatory action. The assessment of decision-making conditions on public policies could be a task accomplished via applicable Law and not only through Political Science. However, this entails work using an appropriate analysis model to deal with the complex social relations that characterize a regulatory State.

This analysis model should make possible to evaluate the design of institutional regulatory organs and their relationship with the Executive Power (direct Administration), the Legislative Power and the Judicial Power beyond the liberal democratic notion that assumes a static relationship between the preceding Powers. Also, it would be a model capable of evaluating institutionalized decision-making proceedings assuming these proceedings as a means to democratic control and public deliberation upon relevant policy-related matters that are at the root of the selection of administrative techniques to regulate the economy and social life – i.e. the very definition of regulatory content.

And the definition of regulatory content determines material conditions of distribution of resources and stipulates the exorcize of rights by regulation-affected participants. In other words, the choices made at market regulation formulation time will ultimately establish the relevant conditions for social and economic development.

This is the reason why it is critical to evaluate the conditions for democratic control of the internal decision-making processes of the State's own bureaucracy (i.e. the institutional design of regulatory organs and the administrative process, as well as the political dynamics of decision-making processes).

Finally, the model must be able to evaluate participation conditions in the Brazilian public sphere. It has to be able to recognize the relevant public (i.e. interest groups) that takes action on agencies to influence regulatory content and how the decision-making process has become important to analyze the conditions of democratic legitimacy in connection with the planning of sectorial public policies in post-State reform Brazil.

The dominant analysis models in Brazilian law doctrine as regards administrative law and economic law are not, to my understanding, enough to encompass highly complex regulatory State functionings and, more importantly, the legitimacy of the decision-making processes on public policies in a context of legislative delegation (or of exercised conjunctural normative ability) by regulatory organs provided with decision-making autonomy. Those are models still connected to a concept of liberal rights focused on the adequacy of rationale-formal analyses of norms in a hierarchically constituted legal system.

On the other hand, the analysis models formulated in the Brazilian theoretical social-political debate end up being insufficient as they tend to display a restricted notion of both, democracy and accountability. Otherwise, they are either bound to models of liberal democracy – rooted in the understanding of social relations based on methodological individualism focused on the concept of purely instrumental reasonableness – or tied to an extremely idealized republican ideal of democracy – requiring high level citizenship and public sphere dynamics which at times are incompatible with actual organization conditions of the civil society.

In the abovementioned models, accountability is seen as control of the administrative output (in terms of

performance), centered in the electoral process (vertical accountability) as regards responsibility, or in a relationship of checks and balances among the three Powers seen as exceedingly mechanical or static. On the other hand, this is now being conceived so as to include the dynamics of interest groups from the civil society, but due to its marked republican concept it does not emerge as a solution for substantive questions of democratic legitimacy.

The abovementioned questions inspired a group of young researchers connected to the Rights & Democracy Nucleus at CEBRAP in the FAPESP context of a thematic project coordinated by Professor Ricardo Terra (Philosophy - USP) and Professor Marcos Nobre (Philosophy - UNICAMP) to study the Brazilian state reform experience and related changes in administration techniques with regard to economic and social regulation.

The event Economic and Social Regulation, Accountability and Democracy *was organized by members of the Rights & Democracy Nucleus at CEBRAP - Mariana Mota Prado, Jean Paul Rocha, Rafael Oliva, Diogo Coutinho, Tiago Cortez, Paulo Todescan L. Mattos - in addition to one researcher that was then completing his JSD at Yale Law School - Caio Mario da Silva Pereira Neto.*

The contagious enthusiasm the members of this group demonstrated was vital to make possible to assemble during two days of intense academic debates knowledgeable representatives of different currents of thought from the North American, European and Brazilian debate.

In addition to PhD dissertations on the relevant theme from members of this group completed over the last two years or in final stages of preparation, the same group organized a collectanea of classical texts on Economic Regulation and Administrative Law that was published by Editora 34 *on the date of the conference under the title* Regulação Econômica e Democracia: o debate norte-americano[3]. *An additional collectanea containing referential texts from the European debate on the relevant theme was also put together and and will soon be published by* Malheiros Editora.

The carrying out of this conference was a result of the academic output of this group and more speficically the outcome of four years of intense debate at the Rights & Democracy Nucleus at CEBRAP, coordinated by Professors Ricardo Terra and Marcos Nobre - core motivators for the transformation undergone by the legal academic output produced by my generation.

Also essential for the carrying out of this event was the support received from Yale Law School, Fundacao de Amparo à Pesquisa do Estado de Sao Paulo and the Escola de Direito de Sao Paulo da Fundacao Getulio Vargas.[4]

Professors Ary Oswaldo Mattos Filho and Antonio Angarita kindly opened the Fundacao Getulio Vargas for this young group of Law researchers.

The results of the conference on Economic and Social Regulation, Accountability and Democracy *included, in addition to intense debates that typified researchs then being carried out the group, the production of eleven innovative papers by scholars from schools and advanced research institutions from Brazil, USA and Europe. In addition to the foregoing unpublished works, Professor Bruce Ackerman, acknowledged as one of the main North American experts on Constitution brought to our debate the article* The New Separation of Powers, *a challenging work already published in the* Harvard Law Review[5].

*With the creation of a magazine (*GV Law Review*) at FGV's Sao Paulo School of Law an excellent opportunity is now available for publication of innovative papers especially prepared for the Conference.*[6] *The works will be published verbatim as they were submitted to the audience during the debate. The reason they are written in English language is because they were all prepared for an international conference.*

Their publication in the GV Law Review *will allow not only the access by students and researchers to debates and relevant themes and issues discussed thereat, but also the start of new ground-breaking Law research in addition to the continuation of works we endeavored to initiate at the Rights & Democracy Nucleus of CEBRAP.*[7]

The brief description of works presented hereinbelow is in the same order as in the presentations and debates throughout the Conference and consistent with the Conference's Agenda (see Agenda copy below):

Fernando Limongi

Institutions, Presidents and Agencies

The author presents a review and critique of studies and analysis methods on comparative functionings of political institutions. In particular, the North American neo-institutionalistic debate would not be sufficient to explain specificities of the Brazilian legislative process or the relationship between the Executive Power and state bureaucracy. At this point the author establishes a key dialogue with Bruce Ackerman's work, The New Separation of Powers, *which would end up generalizing the diagnosis of the functioning of political systems from the diagnosis*

indicated by a specific analysis model on the functioning of the North American political system.

Leonardo Avritzer

New Public Spheres in Brazil: Local Democracy and Deliberative Politics

The author presents characteristics of the process of expanding participative experiences in the decision making process regarding the subject of public policies in Brazil. The focus of this work from an empirical viewpoint is on participative budget experiences. Based on analysis of empirical experiences the author discusses democratic gains and shortfalls resulting from the participation of participants affected by the content of the relevant policies object of public deliberation. Finally, the author highlights specificities of Brazilian public sphere dynamics stressing difficulties that result from different types of participation by the public, with focus on tensions between participation and deliberation (or between the types of measurement of democratic gains resulting from mere participation without voice or a participation with voiced deliberation).

Charles Sabel

The author, more than a conclusive paper, prepared an agenda for research on dynamic public sphere functioning and its relationship with decision-making processes in the area of public policies. In the proposed research agenda the author encourages debate upon limits of the understanding of the democratic process of making norms restricted to the functioning of Legislative Power and the Administration, as it was understood by theoretical models that attempted to construe the North American state reform characterized by the New Deal *or the European reform characterized by the establishment of institutions that shaped the administrative sphere of the European Union. In addition the author draws attention to dynamic specificities of Latin American state reforms, Administration functionings and the public sphere of a country such as Brazil (establishing a bridge between Leonardo Avritzer's work and his own work) as compared to the North American and European cases.*

Julia Black

Proceduralisation and Polycentric Regulation

in her article the authoress discusses, based on a dialogue with European and North American academic literatures on deliberative democracy, the difficulties met due to the introduction of decision-making deliberative processes on the definition of regulatory content. In particular, the authoress highlights hurdles attributable to tensions between different communicative rationalities and therefore, to public understanding of technical aspects of the relevant regulatory content. Taking into account requirements resulting from the deliberative democracy model the authoress discusses procedural mechanisms of translation and dispute resolution involving technical problems, which would meet challenges derived from the introduction of deliberative processes in the formulation of technical norms.

Fabio W. Reis

Deliberation, Interests and Pluralism

The author presents a critique of presuppositions of the deliberative democracy Habermasian model and underscores tensions between communicative action of which the rationality seeks understanding based on free argument, and the instrumental rationality that would characterize the process of defining technical norms during the practical functioning of institutions. Nonetheless, at a theoretical level the author emphasizes problems of legitimacy and efficacy (understood as efficiency) of the technical norms and attempts to demonstrate the limits of the deliberative democracy model, for improved understanding of the definition of regulatory content in view of the non-existence of an ideal communicative situation aimed only to understanding.

Jerry L. Mashaw

Judicial Review of Administrative Action: Reflections on Balancing Political, Managerial and Legal Accountability

The author focuses the theme of judicial review of administrative decisions and analyzes the role of judicial review as a mechanism for democratic control of the Administration (beyond the role of the Legislative Power) and of the protection of rights of citizens affected by regulatory content. Additionally, the author discusses problems inherent with judicial review in regulatory context, especially because the relevant organization does not consist of elected members and, on the other hand, it does not hold specialized technical knowledge as the regulatory departments of the Administration do. Taking into account judicial control requirements and the difficulties derived from this kind of control, the author reflects on conditions and limits of judicial control with regard to administrative decisions.

Jose Reinaldo de Lima Lopes

The Traditional Dialogue Between Law & Economics

The author establishes a discussion at theoretical level on the tension that exists between legal reasoning and economic reasoning. The limits and conditions of the introduction of economic reasoning in the process of regulatory content are discussed here. At the same time by recalling illustrative examples of the history of institutions operations, the author brings to light the specificity and autonomy of the legal system with its own reasoning of operation in spite of the existing relationship with the economic system. Finally, the author proposes an agenda to research conflicts between regulatory content decision-making processes internal to regulatory agencies, and the judicial review of administrative decisions.

Marcus André Melo

Institutional design, normative political theory and accountability

The author discusses the functioning of political institutions and their democratic control exerted by citizens, particularly focusing on electoral process with the classic mechanism of modern mass-suffrage democracies of veto or confirmation of the politician-elect upon completion of his/her term of office. In the case of creation of institutions that move away from the dynamic of electoral processes - as in the case of regulatory agencies provided with decision-making autonomy - the democratic control of administrative decisions becomes a complex task. The author analyzes to a theoretical level the conditions for democratic control - i.e. accountability - of political institutions considering the relevant institutional design and its position concerning articulation with citizens/voters.

Susan Rose-Ackerman

The Challenge of Poor Governance and Corruption

The authoress discusses governance mechanisms for the operation of institutions - including regulatory organs - that could reduce motivation for corruption. Accordingly, the focus is on corruption problems and highlights Administration operation difficulties. The risk of corruption and mal-function of administrative organizations would be linked to numerous factors, but the control of Administration and markets regulation, mainly by way of accountability with justification of measures taken can help reduce factors that lead to corruption. The authoress presents examples of programs and governance mechanisms that can be adopted to fight corruption and for improved performance of administrative organizations.

Edmund Amann and Werner Baer

From the developmental to the regulatory state: the transformation of the government's impact on the Brazilian economy

The authors present an analysis of the transition from the growth-oriented State model that characterized Brazil from 1930s to 1980s to a regulatory State model characterized by State reforms implemented in the 1990s. The new role of the State as regulator agent is analytically discussed based on examples of public policies on privatization and regulation of Brazil's electric power and telecommunications sectors. Finally, the authors discuss challenges faced when an attempt was made to resume growth-oriented policies - to some extent planned by the Lula Administration - in view of the dynamics of markets regulation and regulatory instruments that became available after reforms implemented in the 1990s.

Luciano Coutinho

Regulation and Development: Reflections in the aftermath of Neoliberalism

The author discusses presuppositions of the State's neoliberal model that characterized reforms made during the 1990s combining both, privatization and incentivated competition, as ends in themselves. The author judiciously analyses competitive regulation of markets and takes into account structural specificities of each market. Particularly in the cases of markets characterized by substantial economies of scale, as infra-structure and public services, or, more importantly, markets with natural monopoly characteristics, the privatization-competition-regulation combination would be neither suitable nor sufficient for sectorial economic development

The Agenda of the event is presented hereinbelow that the reader may understand the different contexts in which each paper was discussed and who were the moderators participating in the event to establish counterpoints between texts and debates with the audience throughout the conference

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Panelists

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Moderator

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Regulation and Economic and Social Development

Moderator

Calixto Salomão Filho *(Professor of Law at University of São Paulo - USP)*

Panelists

Edmund Amann *(Professor of Economics, School of Economics, University of Manchester, UK)*

Luciano Coutinho *(Professor of Economics at University of Campinas - UNICAMP)*

NOTES

1 Doctor of Philosophy and General Theory of Law from USP (Universidade of Sao Paulo), member of the Rights and Democracy Nucleus at the Brazilian Center of Analysis and Planning (CEBRAP), Professor at the Program of Specialization in Law of the Getulio Vargas Foundation (FGVSP).

2 The English word accountability has been translated into Portuguese as responsabilizacao, prestacao de contas or, responsabilizacao com prestacao de contas. However, the use of this word in English literature in areas of Social Science seems broader to me. It is not uncommon in this literature the use of the word accountability to qualify types of democratic control of political institutions.

3 Paulo Todescan Lessa Mattos (coord, et alli). Regulacao Economico e Democracia: o debate norte-americano, Sao Paulo: Editor 34, 2004.

4 The support received from the American Consulate General in Sao Paulo city is also worthy of mention, without which the Conference would not have been possible.

5 Bruce Ackerman, "The New Separation of Powers" in Harvard Law Review, volume 113, January 2000, number 3.

6 Therefore, with the exception of the text "The New Separation of Powers".

7 This event was the second event organized by researchers of the Rights & Democracy Nucleus at CEBRAP in collaboration with Fig's Sao Paulo School of Law . The first event was "What is Law Research?, carried out at the end of 2002, which transcription of debates was published by Editor Quarter Latin at the end of 2004. With the present publication the outcomes of both events became more accessible to the public. I express gratitude yet again to José Rodrigo Rodriguez, Research and Publishing Coordinator at Fig's Sao Paulo School of Law, for having made possible those publications.

INSTITUTIONS, PRESIDENTS, AND AGENCIES

Fernando Limongi

I Introduction

The editor of the *American Political Science Review*, the most prestigious and important political science journal, introduced Jon Elster's review of the book *Analytic Narratives* with a note of enthusiasm about the dissemination of the rational choice approach in political science:

> The rational choice revolution in political science began in American politics in the 1970s, first influenced international relations in the 1980s, and made its way to comparative politics during the 1990s. As it moved beyond its base in American politics, rational choice theory confronted comparative and historical questions of regime transition, social conflict, democratic stability, economic development, and international governance (Vol 94(3), September 2000).

In this paper, I critically review part of this history. I discuss neo-institutionalism since it was through neo-institutionalism that rational choice established itself in American politics. Originally, the approach dominated the Legislative Studies area. From there it made its way to comparative politics. My discussion concentrates in these two sub fields: American politics and comparative politics. (For comparativists, international relations can be ignored). In a sense, and this is one of the points I want to make in this paper, the comparative field has been strongly influenced by the Legislative Studies approach. The consequence is that the comparative field is not prepared to discuss State reform. Ironically, as regulatory

agencies made their way into Latin America, comparativists were not prepared to discuss their impact.

Practitioners of comparative rational choice neo-institutionalism seem to be proud with their achievements. They are prepared to move on, to conquer new subjects. For instance, one reads in the introduction Haggard and McCubbins (2001 1) wrote for a recently edited volume

> A generation of work has shown that institutions affect various political outcomes. For example, numerous scholars have shown that electoral systems shape the behavior of parties, candidates, and voters. Other scholars have demonstrated that different constitutional structures, such as presidential or parliamentary systems, affect regime stability, accountability, responsiveness, and democratic durability.

I am not so sure that what was supposed to have been shown or demonstrated has really been done. There is no doubt that the variables cited —electoral laws and the form of government—have been the working horses of the neo-institutionalist comparative field. However—and this is a point want to make—substantive findings have not been established on solid grounds. This paper main objective is to substantiate this assertion. The demonstration asks for three sections, followed by the concluding remarks.

The second section is dedicated to a brief incursion on methods. My objective is to show that what is proudly taken as the founding stone of the movement, the proof that institutions induce stability on collective choice, is not such a big achievement. The problem the 1979 celebrated Shepsle paper solves is, at most, an interesting theoretical question. It makes sense in one tradition of though: the so-called social choice approach. This approach precedes the advent of noncooperative game theory as the standard formal modeling technique. In the noncooperative approach, though, the question that obsessed scholars in the early seventies–why so much stability when the theory predicts instability— vanishes. Hence, one cannot say that institutions matter because they induce stability. This is not enough. One needs a lot more. One needs to establish that different outcomes follow from different institutional arrangements. This, I argue, is a much more difficult task.

The third section is dedicated to the reconstruction of the core of the rational choice institutionalism applied to American Politics. I present a very simple review. I do not intend to present an original reconstruction. Quite the opposite. I want to present a non sophisticated review because I believe that it is this non sophisticated view that made its way into comparative politics. True, I construct a sort of a straw man argument, but my point is that it is this straw man that has traveled abroad. At the end of this section I present a summary of the assumptions and premises that "invaded" the comparative field.

The fourth section is dedicated to a brief discussion of the effects –or the alleged effects—of the forms of government over public policy. I take this debate because of its importance for the field. Moreover, I use this discussion to illustrate some of the findings of the previous section. My conclusion is that it may well be the case that parliamentarism outperforms presidentialism. Yet, so far, we do not know why.

The fifth section is dedicated to the discussion of presidentialism and bureaucratic agencies. In reality, I have little original material to present in this section. I have to confess that time constraints forced me to conclude the paper before I could really finish it off. The paper is a work in progress. I just present an outline of what should be an independent section dealing with presidential power and bureaucratic agencies. I intend to develop this section to include an empirical analysis of some aspects of the Brazilian state reform. The definitive version of the paper will have a discussion of the independent agencies created during Fernando Henrique Cardoso's administration.

Concluding remarks close the paper.

II Methods and some preliminary comments

To start with, one needs a definition of institutionalism. Diermeier and Krehbiel (2002 4) parsimonious definition is a could place to start:

> The method in this kind of research consists of analysis in which institutional features are taken as exogenous and behavioral postulates are fixed, and then compares equilibria that are generated under different institutional arrangements.

The definition is simple and clear. It is a useful point of departure to avoid an infinite regress. If institutions are taken as exogenous, then one does not need to explain its emergence. One might do it, but it is not necessary. For the authors, if one wants to explain the emergence of a given institution, then one need to step back and start from a given set of institutions to derive the emergence of "the second order institutions" of interest. Obviously, behavioral postulates should be kept constant. As the authors dub it: this a Russian doll approach.

Although simple, this definition leaves on the side the questions usually associated with the onset of the movement, the Arrow's impossibility and McKelvey's chaos theorems. The problem is not to explain why the choices collectivities make are stable. One does not need to reason from the state of nature. In fact, if considered seriously, the world imagined by Arrow and McKelvey is not really a non-institutional one. In both cases, it is the specific institutional set up, the fact that one can always introduce an alternative to be voted against the status quo, that generates instability.

The Structure Induced Equilibrium (SIE) tradition emerged from social choice theory inheriting its methods and research agenda. The research agenda was motivated

by what leading institutionalists have tended to refer as "the spell of Arrow and McKelvey", meaning the lack of majority voting equilibrium in multi-dimensional settings. The equilibrium concept used was the core: a point that once chosen could not be defeated by majority vote. However, this tradition did not rely on a clearly established behavioral postulate. The properties of the core were the object of the inquiry. Why would that point be the one chosen was not part of the inquiry. For instance, the McKelvey result relies heavily on myopic behavior.

Austen-Smith and Banks (1998) refer to such approach as the "preference aggregation approach". One just aggregates preferences under different rules and compares results. What is missing, as noted by Austen-Smith and Banks (1998 261), is the connection between preferences and actions. To return to McKelvey's result: the power of the agenda setter to move the collective choice through the whole space depends on a series of binary preference relations. In the usual textbook example of this theorem, all but the agenda setter end up worse off at the end of the sequence of votes. In the textbook example, players would be led to that Pareto inferior outcome through a series of cleverly chosen sequence of choices, as if they were actually voting. But, the proof of the theorem does not rely on actual voting. No one votes. Actually, no one does a thing. It is only a possibility. That may happen. Is it likely? The answer for the scholar trained in the non cooperative approach is no, this will not happen. The same holds for Arrow.

Hence, the two theorems do not have an empirical content. They cannot be read as predicting this or that will happen. The point is, to return to Diermeier and Krehbiel, there is no behavioral assumption to link preferences and actions.

The solution proposed by Shepsle (1977) to the so-called chaos problem is not difficult to understand. The key operation is the partitioning of the "multidimensional choice space into subsets of single issues that are voted on one at time". In so doing, the problem posed by the multidimensionality reduces to a series of choices in a one dimensional space. Since for the one dimensional case, provided that some conditions hold[1], one can apply Black's median voter theorem, the partitioning of the space is an essential step for the solution. The second part of the solution is also obtained by a crucial assumption, namely, the separability of the issues. That is, the decisions in one issue (one dimension) do not affect and/or are related to the ones taken in another issue (dimension). Diermeier and Krehbiel (2002 16) note:

> The key methodological idea of SIE theory thus consists of transforming a social choice problem in which the core does not exist (multi-dimensional choice spaces) into a more structured problem in which the core does exist. Note, however that such strategy maintains the core as the equilibrium concept.

The solution Shepsle proposes has a correspondence with real world institutions. The partition of the choice space corresponds to the way the American

Congress organizes its decision-making process via a committee system. But, as a social choice model, the proof says nothing about the working of the Congress. Shepsle proves the existence of the equilibrium. The model doesn't say a word about how the identified point will be reached in the real world situation. There is no action. No one chooses or votes anything. So institutions here matter but they matter in a very specific way. All they do is to aggregate preferences in a straightforward way. Descriptive and empirical analysis, to be discussed in the next section, is not directly related to the proof.

The SIE approach has its roots on social choice and cooperative game theory. For two decades or so, noncooperative game theory has been the dominant approach in the field. The superiority of the latter, according to Diremeier and Krehbiel, stems from its equilibrium concept (Nash equilibrium) and its behavioral postulate (individuals always choose their best-response strategies). For the argument put forth in this paper, two consequences of the noncooperative approach deserve special mention.

First, as Austen-Smith and Banks note (1998 274), the cooperative and the noncooperative approaches have opposite consequences. While the problem with the social choice approach was the lack of a core, for the noncooperative game theoretic approach the problem is opposite: too many equilibrium. Hence, "in this respect the concept of Nash equilibrium is too weak; it places few restrictions in what outcomes might be observed".

Second and to make things even worse, results are sensitive to the specific aspects of the game. Diermeier and Krehbiel (2002 19) take this feature as positive:

> The qualitative features of the Nash equilibria are highly sensitive to the precise details of the game forms. From the very beginning this fact precludes any notion of an 'institution-free' theory. Rather, the potential fruitfulness of the game-theoretic approach stems from the simple fact that it explicitly models some features of political institutions, and therefore, highlights *how* and *why* institutions matter

However, as Kreps (1992 94) noted, the dependence on the model specification cuts both ways. True, one may be able to compare different results as one varies the institutional set up. But it also means that game theory "requires models of competitive interaction that are very exact and precise as to the strategies available to the players". Some interactions may not provide such clarity. Besides, the way the modeler conceives the options available to the actors may drive the results. Hence, predictions depend heavily on the way the modeler translates the real world situation into a game form.

Hence, the apparently simple approach proposed by Diermeier and Krehbiel raises a series of problems for neo-institutionalism understood as a method. Can such an apparent parsimonious method provide us with clear-cut answers? Will the

analysis provide the analyst with a restrict set of meaningful outcomes to compare? Will the political process generate different outcomes as institutions differ? Will the results depend on the way the model restrict the actors' options?

All things considered, what comparativists take as the great achievement of neo-institutionalism —the 1979 Shepsle proof that institutions induce equilibrium—-is not such a big achievement. It cannot be taken as the founding stone of institutionalism. The field research agenda cannot be defined by the search of equilibrium or stability. The real problem with institutional analysis is quite the opposite. To quote Kreps (1992 95): one has "too many equilibria and no way to choose" among them[2].

III American Politics: legislative studies and the distributive approach

Rational choice took over the American politics field carrying the neo institutionalism flag. As far as policy predictions were the concern, the claim that institutions matter had a clear meaning. The democratic process leads to distributive policies. Costs are dispersed and benefits are concentrated. Hence, from the substantive point of view, the first vintage of American politics of neo institutionalism is associated with the distributive approach and its application to the study of legislatures.

At first sight, the distributive approach to congressional politics seemed to fulfill the promises of neo institutionalism: one could predict outcomes from assumptions about individual behavior and a precisely defined institutional set up.

Fiorina and Noll (1978 256) establish in a comprehensive and direct way the point of departure of this type of analysis:

> We assume that in choosing among alternative political actions, voters, bureaucrats, and politicians pursue their self-interests. For voters, this means casting votes in a manner that maximizes expected utility, given the platforms of competing candidates. For bureaucrats, this means maximizing some measure of the size of bureaucracy. For politicians, this means maximizing the probability of election.

As Shepsle and Weingast (1984 345) explain, for members of Congress, the reelection goal translate into a specific strategy:

> Members of Congress, at least since the turn of the century, have been motivated by two strong desires: to secure reelection by serving their constituents and to develop a personal power base in Congress. That is the system. Moreover, to strengthen their power bases and to provide for constituents, members have, with considerable success, altered the very ways Congress conduct business. In so doing, they have produced a policymaking machinery that often serves more general public purposes only as an incidental by-product of these political objectives.

Members of Congress use their mandates to pursue their objectives. As a member of Congress, representatives may design policies that help themselves to obtain their objectives. This is the secret. It explains why representatives have been so successful in the electoral arena. It has been accepted as an uncontroversial fact that reelection rates are very high in the US Congress. An incumbent defeat is a rare event. Party swings and presidential coattails also lost their importance. The Representative, no matter his or her party, is alone, is responsible for his or her electoral fate. It all depends from his or her capacity to use the mandate to develop a personal electoral basis.

The description of the institutional set up that favors the attainment of this objective is well known. The Legislative decision making process is organized around the committee system. Committees have well defined policy jurisdictions over policy areas (say, agriculture, industry etc). Bills are reported to one and only one committee that has the monopoly over the legislative initiatives in its jurisdiction. Hence, the status quo in a given area cannot be changed without the initiative of the committee.

Representatives choose the committees they want to join without any control from the parties or the leaders. They self-select themselves into the committees that have some say on what matters for their district. That is to say, electoral considerations drive the distribution of representatives through the different committees. It follows that committees are composed by "preference outliers". That is to say, the preferences of the committee members on the issues that are under its jurisdiction are more extremist than the ones of the floor. That amounts to say that committee members will favor an activist role of the state in the area under its jurisdiction. At least, a much more activist state than the median floor representative would want. To sum up, this is a model in which minorities rule.

Committees (and the sub-committees, in some accounts) are the key actors to define the outcomes of the decision-making process. Their members' interest define the policy congress adopt. In this set up, committees are the real centers of power. The match of the socio-economic characteristics of the district with the committee jurisdiction plays a central role in the argument. As Shepsle and Weingast (1984: 350) put it:

> Policies, as a consequence, are victimized by two territorial imperatives emanating from the legislative branch – geography and jurisdiction, constituencies and committees – which help explain the past decade's growth in federal budgetary commitments.

In other words: programs and policies will be tailored to attend the interests of those seating in the committees (or sub-committees). Given the self-selection appointment norm, these members are the ones with high stakes on the areas

under their committee jurisdiction. The committee controls the policies that matter for the district.

Although, committees are not representative of the floor, the floor will approve policies the bills the committees report. Why and how they do so, it is not clear. At least, there is no institutional foundation for such voting trade (Krehbiel 1987). One non-institutional explanation is deference. The floor recognizes the superiority and the greater specialization of the committee. It has also been argued committees trade votes among themselves. The line is: as long as the others vote for my most electoral profitable policy, I will vote for theirs. But this is only one among many other possible outcomes and one needs more than a plausible story.

This point deserves emphasis: the model misses a key element. There is no explanation for the floor behavior. The floor has no rational basis to delegate power to the committee. The point missing is related to problem identified with SIE. There is a behavioral postulate missing. If the relation of the floor with the committee follows the standard noncooperative assumption, no such a delegation should happen. Although this criticism was raised at the onset of the movement, it contributed little to decrease the influence of the distributive approach[3].

In this set up, the floor does not deliberate. Given the supposition that committees are composed by "preference-outliers" with homogeneous preferences, committees do not deliberate either. The decision making process is a mere aggregation of pressures emanating from the districts.

The consequence of this type of committee power to the budget, as Shepsle and Weingast (1984: 353) put it, is obvious: "there is a predisposition to increase spending". Overspending –or an interventionist state-is accompanied by a greater attention to the district needs and a lesser attention to the national interest. In fact, given the politicians' objective and this institutional set up one can predict all sort of inefficiencies in the programs congress approve. For instance, since a new program must gain majority support, Congress will prefer programs that spread benefits across many districts. The consequence for Shepsle and Weingast (1984 358) is that

> too little of the program is achieved relative to the amount of resources spent. In some cases (such model cities), this transformation may be so complete that is not clear whether the program's objectives are achieved at all!

Another inefficiency, according to the same authors, comes from the bias in favor of programs that follow a political and not standard cost-benefit economic analysis. This implies the possibility of divergence between the two criteria, the political and the economic. In fact, one can reason that politicians will prefer programs that are larger than the ones economists would choose. Economic costs may be transformed into political benefits. The number of jobs created by a program provides a good

example. Jobs are politically relevant inputs for politicians struggling for votes. Over-contracting may bring more votes. The same logic applies for the search of the suppliers of intermediaries products. Politicians will favor district suppliers, with no regard to its efficiency. Examples could be multiplied.

As a pattern, public policy will take the classical distributive form. A distributive policy, to follow Fiorina and Noll (1978 256) definition, is one that

> is divisible into subactivities, each of which is evaluated and decided upon separately and is beneficial to a relative small proportion of the electorate. Examples are federal constructions projects, categorical grants, and commodity-specific tariffs.

The "electoral connection" imposes a political logic toward state expenditures. Politicians favor distributive policies because those are the ones that provide the best electoral return. For the constituency, the representative appears as the providers of goods, services and programs. Of course, voters pay for these state services. But the payment is diffused via the tax system that applies to all and, besides, is confusing. Costs are spread. Benefits are concentrated.

The "conspiracy" between geographic (the districts characteristics) and the jurisdictional committee control over policy areas tell us the whole history. We know the structure of the incentives politicians have and we know institutions pose almost no constrains on the ways their goals may be pursued. They hide the costs and provide concentrated benefits for voters in their district. This "conspiracy" explains policies after all "the method of producing some public goods or service, and consequently the incidence of spending, is endogenous -it may be selected for its political consequences" (Shepsle and Weingast 1984 356).

There are other conspiracies to consider. There is a "conspiracy" that matches the committee with the bureaucratic agency. Politicians do not provide the benefits themselves. They need the help of bureaucrats. For the bureaucrats, as we saw above, the greater the bureaucracy, the better. Thus, there is space for politicians and bureaucrats to collude around the level and type of services they provide for voters. It is easy to see that they are in condition to choose services that are beneficial for both. In short, as Fiorina and Noll (1978 257) argue

> Legislators and bureaucrats have an incentive to provide government services in an excessively bureaucratized manner. To do so raises the demand for facilitation services (...) As the public bureaucracy grows larger, the importance of the performance of facilitation will grow, and a legislator who is a good facilitator will be increasingly likely to be reelected. A challenger who is unproven as a facilitator is a riskier choice than an effective incumbent, and consequently provides a lower expected payoff in this role[4].

There are too many versions of this argument. One may also take it from a different angle and include the "special interests" into the picture. The expressions coined to grasp the essence of these descriptions are well known: "policy subsystems", "cozy triangles" "whirlpools", "subgovernments". The accent may change from one approach to the other, but the thrust of the argument remains the same.

For the rational choice view, the first point to emphasize is that these actors - politicians, bureaucrats and special interests—are in equilibrium. Morris Fiorina (1989 122) makes the point clearly in the following passage:

> Committee members enjoy the opportunity to exercise great influence in a particular area—given the pattern of committee assignments, often an area of considerable concern to their districts. The agency receives support from the committee. The clientele gains benefits from the program, and the circle closes when the clientele provides support for friendly committee members. Heterogeneity of interests across districts and states underpins the system. One congressman cares about federal water projects but not federal workers, while another congressmen has the opposite concern. Both are politically better off if they implicitly trade for the right to exert disproportionate influence in the area of greater concern.

Note the choice of words. Fiorina does not say that voters receive the benefits in the district. One may read *clientele* meaning voters or special interests. Special interests may finance campaigns. Hence, the ambiguous term *clientele*: voters or special interests are the same. According to widespread view, voters may be bought or fooled by campaigns.

Hence, committees govern. The floor delegates to committees and committees take full advantage of the delegation. In other words, the business of governing is decentralized and fractionalized. There is no center capable of considering all the consequences of the governmental action. Hence, state policies will lack coherence. This is the problem with the American political system. Once more, Fiorina (1989 4) provides a good summary of this view:

> There is a Washington establishment. In fact, it is a hydra with each head only marginally concerned with the others' existence. These establishments are not malevolent, centrally directed conspiracies against the American people. Rather, they are unconsciously evolved and evolving networks of congressmen, bureaucrats and organized subgroups of the citizenry all seeking to achieve their own goals. Contrary to what is popularly believed, the bureaucrats are not the problem. Congressmen are. The Congress is the key to the Washington establishment. The Congress created the establishment, sustains it, and most likely will continue to sustain and even

> expand it. But I emphasize again that the disturbing aspects of the Washington establishment follow from the uncoordinated operations of the overall system, not from any sinister motivation of those who compose it.

There is a clear parallelism between the interpretation Fiorina puts forth in the two passages I just quoted and the interpretation of the interest group pluralism school, as for instance Theodore Lowi. Several other views reach similar conclusions. One may wonder if other than the method, rational choice did offer a novel interpretation of the working of the American political system. The contribution is subtle but it does exist. To establish the contrast between these two accounts, I quote a passage in which Lowi (1979 74) is describing agriculture programs:

> Due to the special intimacy between federal agriculture programs and private agriculture, each administrative organization becomes a potent political instrumentality. Each of the self governing local units becomes one important point in a definable political system which both administers a program and maintains the autonomy of that program in face of all other political forces emanating from other agriculture systems, from antagonistic farm and nonfarm interest, from Congress, from the secretary, and from the president.
>
> The politics of each of these self-governing programs is comprised of a triangular pattern, with each other supporting the other two. The three points are: the central agency, a congressional committee or subcommittee, and the local or district farm committees. The latter are also usually the grass-roots element of a national interest group.

Democratic government degenerates into the government of the few. Policy is captured by special interests. Delegation of power from the center to the periphery of the system is a common element in these arguments. The debate among these interpretations revolves around the identity of the greater beneficiary: politicians, bureaucrats or special interests. The identity of the great looser is not disputed: the people. Hence, we have a variation of a classical theme. Democracy endogenously degenerates into the government of minorities. The state does not act to promote the interests of the people.

One of the distinctive features of the rational choice institutionalism is to argue that politicians are the greater beneficiaries. At the origins of the movement, lies the discovery of an empirical pattern: the vanishing of the marginal districts. After World War II, reelection rates skyrocketed. Politicians, more specifically, Representatives, are getting what they want. As Fiorina puts it: "Congress is the problem". Congress creates the Washington establishment and benefits from it. Shepsle and Weingast (1984 : 366) assert that it should be so:

> Professional politicians possess ingenuity, an entrepreneurial spirit, and adaptability. Legislative institutions and policies they foster reflect this central fact. Legislators, motivated to secure reelection and legislative influence, devise institutions to further these objectives.

In other words: rational politicians will always devise the institutions' Mayhew hypothetical planners would do: a committee system. Since some may not know the passage —some readers may have other background than political science— this is how Mayhew (1974: 81-2) explains the specific characteristics of the American Congress

> The organization of Congress meets remarkably well the electorate needs of its members. To put it another way, if a group of planners sat down and tried lo design a pair of American national assemblies with the goal of serving members' electoral needs year in and year out, they would be hard pressed lo improve on what exists.

Rational politicians are rational institutional planners. One could do no better. To create a committee system with clear jurisdictional boundaries is the best way to meet politicians' objectives. But, note that this argument goes against institutionalism defined as a methodology. Institutions, if this is the case, do not constrain behavior. Legislators build the institutions that best serve their needs.

As the most basic interest of the politicians –their concern with reelection— explain institutional features and the policy outcome, rational choice approach dilutes itself into a modified pluralism: politicians take the place of the special interests. Besides, methodological individualism takes functionalist tones –after all, institutions are explained by their consequences—a most ironic twist (See Krehbiel 1991).

Let me stress another specificity of the rational choice legislative studies approach: Congress controls the bureaucracy, including the so-called independent agencies. This is a point discussed at length by Terry Moe (1987). As argued by Moe, Congressional dominance is demonstrated noting that committees control the budget, exercise oversight through several devices, and control appointments (Moe 1987 478). There is no need to go any further. I will not present the models employed and/or the fit of the theory with the facts. Moe has already done it and I could not do a better job than him. What I want to emphasize is that is a specific position in a larger debate. The bureaucracy does not control or have autonomy to set up policies. Agencies are creatures of the Congress[5]. The comparative field bought this Congress centered version of the administrative state as if it were the unique one.

As a Congressional centered theory, this approach also reserves a secondary role for the president. In fact, the president is a later comer to the formal modeling of the American political system. For a long period, the legislative studies simply ignored the

role played by the presidency. Her coming to the scene has been recent. Even now, the role the president plays in formal model is a limited one. The presidential power is the power to veto –or to threat with a veto. As Moe[6] has noted, this reduces the power of the president to a simple point in the space, a power that is not much different than the one held by the filibuster senator. Clearly, there is something missing here.

This is a mostly ironic feature. For the comparative field, the choice of the form of government and its consequences is the institutional debate. If institutions were to matter, they should matter in this crucial and fundamental choice. In fact, as the transition literature wanted, the debate over the effects of the forms of government dominated the field. But as I argued above, neo institutionalism was badly equipped to understand the role presidents play in separation of power systems. Not a good start. I discuss this point in the next sections.

To sum up, the Legislative Studies Institutionalism has methodological and substantive features. On substantive terms, it may be read as an interpretation of the way the American administrative state works. It is not a totally original contribution. It shares with other interpretations, the emphasis on the fragmentation of the administrative state. American political system lacks a center that coordinates the action of its parts. As Fiorina puts it: it is a hydra.

It also shares with others interpretation what one may call a populist tone. The big looser is the people. But, legislative studies take the special interests, the president and the bureaucracy out of the main picture. This is, I believe, peculiar to this interpretation. Congress is taken as the center of American political system. The administrative state – an excessively bureaucratized state—is a congressional creature. Hence, the greater beneficiary: the politicians that control Congress. These specific tones have been adopted by the neo-institutional comparative literature. This influence will be the subject of the next section. One may derive all that matters from politicians –in fact from Representatives— interests.

Before closing this section, I want to discuss the role that voters play in this account. One may note that the view I reconstruct relies heavily on politicians' shrewdness. They are able to design the institutions –including the internal organization of the Congress, the electoral laws and the bureaucracy—to serve their electoral needs in a highly efficient way. Voters, as we saw, are the losers. But why would voters let politicians –or the special interests, or the bureaucracy or even the president—behave in this way? After all, aren't voters the sovereign?

Recall that Fiorina and Noll assume that voters are not different than bureaucrats and politicians. They maximize their expected utility as much as the other relevant actors do. Why would they vote for such politicians? Rational voters, one could imagine, could do better than that.

Considerable ingenuity has been devoted to this point. Rational voters are at the foundations of the democratic machinery. The result is not the one they would favor.

The explanation provided by Fiorina and Noll (1987 257)[7] is an ingenuous one:

> The electoral process does not check this tendency because voters face a prisoner's dilemma in choosing among candidates. If voters disapprove of excessive bureaucratization, electing a legislator who attacks bureaucratic inefficiency will be unlikely to alter the outcome of a majority-rule legislature, but will produce a less effective facilitator.

Alternative views have a more negative view of the electorate. For instance, in some accounts voters are considered ignorant with the twist that it is rational to be ignorant[8]. For others, they may be simply bought or convinced of anything via propaganda. In this sense, Fiorina and Noll's view is a benevolent one. They do not attribute to voters insufficiencies the distortion and the pathologies of democracy. Yet, this does not seem to be a good explanation. It is clear that a group of politicians could offer policies that would solve voters' collective action problem. A group of politicians offering these policies –say, a party—would win any election. Clever politicians –and they are very clever on these accounts—would not miss this opportunity.

IV Forms of Government

The form of government figures in the comparative literature as a kind of first principle, *i.e.*, as a variable from which everything that matters can be derived. The variation of the form of government has been associated with the probability of crises, party discipline, economic growth, bureaucratic performance and so on so forth. The argument is well known: the constitutional definition of the powers assigned to the Executive and to the Legislative affect the strategies politicians will pursue. More specifically, it affects the incentive politicians have to cooperate with one another and, thus, with the government.

Under parliamentarism, members of the legislative body have incentives to cooperate with the Executive. This is the essence of the fusion of the executive and the legislative powers. The majority (but see below) of the legislature have their fate associated with the fate of executive. Their mandates are linked to the survival of the government. Under presidentialism, there are no incentives for cooperation. This is a consequence of the very definition of a presidential system: the chief executive and the legislators mandates are fixed and independent. Presidents do not have the weapon Prime Ministers have, namely, to threaten to cut short what legislators care the most: their mandates.

In this section, I review the basic arguments put forth in this debate. I show that the characterization of the presidential system is highly dependent of the legislative studies view of politics presented in the previous section. Politicians –I should say,

legislators—basic interests drive all the argument. I note the logical inconsistency of the contrast build on such basis. I also show that attempts to move beyond this view have not been very successful. The problem in these cases is due to choice of paradigmatic cases. Characteristics of the US political systems are taken as characteristics of all presidential systems. That is, all presidential systems are treated as coequal with the American system. The internal variation of presidential systems is not taken into account. Conversely, the same type of reasoning is applied to England and parliamentarism.

The contrast parliamentarism versus presidentialism is made considering that any form of government faces a majoritarian imperative[9]. Without assembling a majority in the legislature, any government, no matter its form, will not be able to govern. If this is the case, if the government does not have the support of a majority, the political system is deadlocked, faces a governability crisis or you named it.

Parliamentarism, according to this view, is a regime in which the government, in order to come to and stay in power, must enjoy the confidence of the legislature. Since these are systems in which decisions are made according to majority rule, it follows that no government that does not enjoy the support of a majority will exist under parliamentarism. Minority governments could occasionally emerge, but these would be relatively infrequent and necessarily ephemeral occurrences, which would reflect the temporary inability of the current majority to crystalize. This inability is temporary for the system contains automatic correctives for these situations: either a new government supported by a majority will be formed or, if this is not possible, new elections will be held so that such a majority may emerge.

Presidential regimes, in contrast, do not have a built-in mechanism to overcome the majoritarian imperative. Voters, under presidentialism, have two agents who, by design, do not necessarily represent the same majority. These agents have fixed terms in office and do not depend on each other to exist. As a consequence, there is nothing in the system that guarantees that the executive will enjoy the support of the majority in the legislature. If this situation obtains, then the most likely outcome, it is believed, is stalemate and impasse between the executive and the legislative, which can ultimately result in the collapse of the democratic regime.

There are, however, empirical reasons to doubt that one may distinguishes parliamentarism and presidentialism following this line of reasoning. In the first place, as conclusively demonstrated by Strom (1990), it is not true that parliamentary governments will necessarily produce majority governments, and most importantly, it is not true that, when they do not, the minority governments that emerge should be seen as a sign of crisis or of malfunction of the political system. Indeed, according to his and other counts, about one-third of governments in parliamentary regimes are formed even if they control less than 50% of the seats[10]. More importantly, Strom's analysis shows that minority governments are not a function of political

instability or system malfunction. Rather, according to him, the emergence of minority governments can be explained in terms of the calculus made by party leaders about the costs and benefits of participating in government, given that they are concerned not only with achieving office, but also with the policies that are to be implemented by the government and the consequences of holding offices on the next election. This calculus, Strom argues, is affected by the degree of policy influence parties can exert out of the government, as well as the competitiveness and decisiveness of the electoral process[11].

Note that Strom and others account of minority government take into account governments supported by coalitions, that is, situations in which no party controls the majority of seats. Thus, in multi party systems, minority governments are tantamount to failure to form a majoritarian coalition. Hence, that means that there are parties that could but do not hold portfolios. If the politicians' strategies were exclusively driven by their desire to hold office, then this should not happen. One would always prefer to hold a portfolio over not holding one. Yet, as Strom argued, parties may prefer to influence the policies the government chooses instead of gaining the perks that comes with holding a portfolio.

Turning to presidentialism, there is evidence that minority presidents, although frequent, are not as widespread as one would expect them to be. If we count presidential and mixed regimes between 1946 and 1996, we find that in about 61% of the years the party of the president did not control a majority of seats in Congress. This rate is lower if we only consider pure presidential regimes (58%), particularly in unicameral systems (48%)[12].

Obviously, these cases, however, do not occur randomly. As one would expect, the frequency with which the party of the president does not hold a majority in congress increases markedly with the number of effective parties. That is to say, is higher when legislative elections are held under proportional representation systems. But, more importantly, when they occur, minority presidents are not conducive to the breakdown of the regime: presidential regimes are as likely to die when the president controls less than 50% of the seats in congress as when they control more than 50% of the seats in congress.

As to deadlock, it is not the case that it is pervasive and that it is associated with regime breakdown under presidentialism. Note, to begin with, that deadlock will only occur when the preferences of a majority cannot prevail. These situations, however, do not depend exclusively on the share of seats controlled by the party of the president in congress. It also depends on whether the president has veto power; on the type of congressional majority necessary to override the presidential veto; on whether the system is unicameral or bicameral; and whether, in bicameral systems, veto override is by a vote in each chamber separately or in a joint session of both chambers. When these factors are taken into consideration, one can, in fact,

distinguish three situations: the situations in which either the president or the opposition "rules" and the situation in which deadlock may emerge. The latter will only occur when the president is likely to veto a bill approved by a majority in the legislature, but that majority is not sufficient to override the presidential veto. If the president vetoes a bill and the opposition has enough votes to override the presidential veto, then the opposition "rules." If the president signs the bills that were approved by his/her majority in congress, then the president "rules."

Thus, once we consider both the political and the institutional conditions that may generate deadlock, we find that the relationship between minority presidents and deadlock situations is less than perfect and, most importantly, that presidential regimes are not more likely to die when deadlock situations exist.

As to parliamentary regimes, the argument is that deadlock will never occur. Indeed, parliamentary regimes are designed in such a way that whenever there is a deadlock between the government and the legislature, either the government changes or the legislature changes. Thus, although divided government may also exist under parliamentarism (for example with minority governments), divided government in parliamentarism cannot produce deadlock, at least not deadlock in the same sense that we think of it under presidentialism.

Yet, the fact that under parliamentarism there is a mechanism that can be invoked in the face of policy conflict between the government and the legislative majority does not mean that this mechanism will always be invoked, or that, once invoked, it will necessarily put an end to the disagreement that led to its use. In other words, the existence of a mechanism for dealing with conflicts between the government and the legislature does not mean that the conflict will be resolved whenever it appears. For this reason, deadlock may also occur in parliamentary regimes. It will probably assume a different form than deadlock in presidential regimes, but it will nonetheless be present.

One interesting case is suggested by Denmark. The post-1973 period witnessed the emergence of a curious norm regarding executive-legislative relations, which entirely violates what we would expect to see happening under a parliamentary form of government. Before 1973, as Damgaard (1944) demonstrates, governments expected parliament to pass proposals it introduced and not to pass proposals that the government did not want to see passed. Opposition parties would not insist on a vote that would mean a government defeat, unless, of course, "the purpose was actually to defeat the government" (p.31). In line with the "norms of parliamentarism," a government defeat on a vote of some importance would lead either to resignation or to new elections. After 1973, however, but in particular in the 1980s, "the government accepted numerous defeats in more or less important matters without resigning or calling elections." (p.32). Thus, during the "fourleaf-clover" governments of 1982-88, "the government lost every twelfth final division" (p.33):

of 1356 votes taken during this period, the government lost 108 and in 105 of them "it decided to accept the defeat without applying sanctions in order to stay in office" (p.34).[13] Hence, it is not at all clear that parliamentarism guarantees an automatic resolution to disagreements between the executive and the legislative.

Another significant illustration is provided by Greece, where it took three elections and five governments in the short space of 10 months to resolve the impasse that had emerged during the government of Andreas Papandreou. The solution that eventually emerged was itself not perfect: the government that emerged from the April 8, 1990 election headed by the New Democracy party controlled exactly 50% plus one seats in parliament; this government became possible only after the external support of the one member of the center-right Democratic Renewal was secured. It is clear, therefore, that the built-in mechanism available in parliamentarism for the resolution of impasses may fail depending on whether the conflict is a reflection of the distribution of preferences in the population and on the current elite's reaction to these preferences.[14] The point to be emphasized, thus, is that, although at any given point in time parliamentary institutions seem to contain the solution to a deadlock situation, there is nothing that guarantees that a solution will be found.

As a matter of fact, one of the traditional arguments in favor of presidentialism emphasizes precisely the point that parliamentary regimes do not guarantee that there will always be a government (Sartori 1994). Parliamentary regimes will produce stable governments only when some additional political conditions obtain (such as a non-fragmented party system, composed of disciplined parties). Presidentialism, in turn, would be able to produce a government even under very adverse political conditions.

But, so far, one possibility has not been considered, namely that a minority president may count with the support of a party coalition in the Legislature. When no party holds a majority in a parliamentary multi-party regime, the most common outcome is a government backed by coalition. Presidents, the usual argument goes, can rely only on his own party. Coalitional government does not seem to be a feasible alternative.

As an empirical matter, coalition governments are not at all foreign to presidential regimes. The most complete study of this topic is the one produce by Deheza (1997) who considered governments in 9 South American presidential democracies between 1958 and 1994. She found that, of 123 governments observed during this period,[15] she finds that 69 (56%) are coalition governments, of which 24 are minority coalition governments. She also finds that a significant share of coalition governments is formed after the election. There were 59 governments formed as a consequence of presidential elections; of these, 30.5% were coalition governments based on pre-electoral agreements. Of the remaining 41 governments, 17 (41%) were post-electoral coalition governments.[16]

The question that one must ask, of course, is the one about what keeps the coalition together in presidential regimes. In parliamentary regimes, the often cited mechanism that should be sufficient to keep coalitions together is inherent to the regime: the risk that governments will fall if a coalition member defects. This mechanism is obviously absent under presidentialism, and hence parties will face no costs of defecting from coalitions. Although this is obviously a difference between the two regimes, it does not follow that it is sufficient to induce coalition behavior in them. That this behavior is considerably more complicated can be seen from the following hypothetical examples.

Imagine, in the first place, a country with a parliamentary system in which elections are held and no party obtains a majority of seats in the legislature. As a result a (minimum winning) coalition government is formed. A few months into the term some exogenous crisis hits the country and the government is required to implement measures that go against the positions of one of the coalition partners. This party's decision about what to do will depend on which of the two alternatives is less costly to it. It can choose to support the government against its own positions at the cost of promoting a policy that is not its preferred policy and perhaps at some electoral costs in the future. Or it can choose to vote against the government, thus blocking the implementation of policies that it does not like, but paying the cost of facing another election and eventually staying out of office. One can see that the party will choose to support the government only if the costs of anticipated elections are higher than the inherent and future electoral costs of deviating from its policy preferences. There is no reason to suppose that this will always be true. But this is what we have to suppose to believe that parliamentary regimes will necessarily induce coalition governments.

Now imagine a similar situation under presidentialism. Faced with the choice of supporting policies that it does not like, that party does not have to consider the cost of anticipated elections. But it still has to consider the costs of promoting a policy that is not its preferred policy, the eventual electoral costs of this decision, and the certain costs of being out of office. Again, there is no reason to suppose that these costs will be necessarily smaller than the costs of remaining in power and supporting the government. But this is what we have to do in order to believe that presidential regimes will necessarily lack inducements for coalition participation.

Thus, the view that under presidentialism legislators and parties lack incentives to cooperate with the government depends not so much on the fact that this is a system of separation of powers, but on the assumption that all that the actors care about is to come to and stay in office. As I have shown above, if one applies this assumption to parliamentary regimes, one cannot explain, among other occurrences, minority governments. So, nowadays, models of government formation under parliamentarism (see for instance, Austen-Smith and Banks 1988) assume that

voters care for policies as well as for offices. If we hold the same behavioral assumption for presidentislism, then one is forced to conclude that minority presidents are not doomed to fail. If politicians under presidentialism care about policies than they may opt to cooperate with the president. Presidents can form coalitions and govern with its support.

In fact, Przeworski, Cheibub and Saiegh (2002) have show that standard game-theoretical model of government formation under parliamentarism, the one proposed by Austen Smith and Banks (1988), can be accommodated to the presidential institutional set up. The authors show that substantive results do not depend heavily on the form of government. That is to say, if one follows Diermeier and Krehbiel advice, that is, if the behavioral assumptions are kept constant while the institutional set up, and only the institutional set up varies, then the alleged differences between the two forms of government disappear. When one gets differences, it is because the behavioral assumptions vary with the institutions. In the case of the incentives for cooperation, one usually assumes that politicians care exclusively about office in presidential regime and about office and policy in parliamentary regimes.

I could go on. Party discipline would be an obvious issue to tackle now. It is common to argue that disciplined parties are foreign to presidentialism and a necessary feature of parliamentarism. The structure of the argument depends on the absence(presence) of incentives for cooperation in presidential(parliamentary) regimes. So there is no need to go over all these arguments. The objection parallels the one made above. Empirically, the claim is also false. Just consider Venezuela before Chávez and Italy and France Fourth Republic. There are disciplined parties in presidential regimes and non disciplined on parliamentary.

The strategies of the relevant actors, above all politicians, are constrained by several other institutional features. In a sense, forms of government is too macro and general to define strategies. Actually, comparativists do not work at this general level. They do fill in the details and, most often, they derive these consequences from the institutional details of the cases they know better. In fact, to take the United States and England as the paradigmatic cases of presidentalism and parlimanetarism is a common practice in the field.

More than that, one tends to confound traits of the American political system with its form of government, and, to do the same with England.

This is clearly the case, just to illustrate my point, of the frequently cited paper by Moe and Caldwell (1994). The authors pose the following question:

> Take bureaucracy. Would a parliamentary system tend to generate a bureaucracy that is markedly different –in strucuture, performance, accountability—from what we should find under separation of power? (172)

The authors provide a positive answer. Bureaucracies differ as a consequence of the form of government. Besides posing the question in such a general terms, Moe and Caldwell explicitly attempt to base their answer in a deductive mode. The difference follows from the very principle that distinguishes the two forms of governments. As they (1994 172) put it

> When a nations choose a presidential or a parliamentary from, they are choosing a whole system, whose various properties arise endogenously –whether they like it or not—out of the political dynamics that their adopted form sets in motion. Attractive structures of government may be impossible to achieve, unattractive ones impossible to avoid. Presidential and parliamentary systems come with their own baggage. They are package deals.

But, when comes to derive what each system puts in motion, the authors basically describe two cases: the United States and Britain. With regard parliamentarism, they explicitly inform the reader that they will concentrate on the "classic Westminster case" (177). As of presidentialism, the picture is even worse, since their commentaries is not preceded by a similar restrictive warning.

Being schematic, their conclusion is that bureaucracies are less effective under presidentialism than under parliamentarism. But, the conclusion is not derived from characteristics that define these forms of government. In the case of parliamentarism, their argument relies heavily on characteristics of the British system that are not necessarily found in all parliamentary systems: a two party system, highly cohesive parties and "unchecked authority". On their account, this is a system with real power alternation and in which is easy to change the status-quo. Hence, the conclusion: "Agencies and programs cannot be insulated from opponents and future authorities by embedding an intricate ex ante control strucuture in the law" (177). It may be true that given a Westminster system, all these consequences follow. But the Westminster system is not the only form of a parliamentary system. The crucial features from which the bureaucratic characteristics are derived –power alternation and absence of a Constitution—do not define parliamentarism.

The same is true for their argument about the bureaucratic structure under presidentialism. Their argument is based upon the conflict between the executive and the legislative and the way each Power tries to shape the organization of the government. Key for their argument is that both act independently and with different objectives on that matter. Congress colludes with interest groups whereas presidents act unilaterally. Interest group want agencies that do not work since they fear the State and the possibility that an adversary interest group captures the bureaucracy. Hence, they design bureaucratic institutions that do not work. The president wants the agencies that Prime Minister can get, but all he can do is to add a new layer of agencies over

the ones Congress and groups have already created. Thus, although presidents are "the only champion of effective, responsible government", their efforts and initiatives end up contributing to "create still more bureaucracy and heighten complexities and internal contradictions of the American administrative system" (176)

The conflict over the control of the bureaucracy is not a necessarily feature of the separation of power systems. Not all presidentialisms are like the American. Separation of power does not necessarily imply that Congress and the President will dispute the control over the bureaucracy.

Moe and Caldwell are not alone on trying to relate forms of government and bureaucratic performance. Other attempts incur in the same mistake: to confound features of the US and of the British system as if they were necessary aspects of the forms of government they adopt. For instance, Ackerman (2000 695) argues that parliamentary regimes foster functional specialization: a bureaucracy that knows that it will have to serve different masters along the road will want to "cultivate a reputation for neutral competence. Whatever goals have been established by the cabinet, the senior civil servant stands ready ad eager to implement them." The premise of the argument is that the "PM and her cabinet ministers have their eyes firmly fixed on the next elections. If they loose, then the fate of all their precious legislative initiatives is at mercy of their political opponents. As a consequence, they want knowledgeable and effective implementation from the bureaucracy, and they want it fast". (695). In this world, bureaucrats have to prove that they can provide the solutions both sides want fast. Hence they don not take sides, they are neutral and want to prove their competence. That would make them more valuable.

Again, a two party system with clear-cut rotation and in which the status quo can be changed at the majority's will with few constrains are not characteristics of the parliamentary system. In Italy and Japan, one party controlled the government for forty years or so. Even in England, rotation in power has not been as fast as assumed by the argument. The conservatives held power for fifteen years or so, and the Labour has been in power for almost ten years. In fact, this tantamount to hold constant the variables Strom (1990) invokes to explain minority governments: the competitiveness and decisiveness of the electoral process. Besides, under coalitional government, the standard argument goes, voters do not know which party should be held responsible for government performance.

The critical assessment of the American bureaucracy Ackerman offer does not extend to all separation of power system. American bureaucracy, according to Ackerman, is highly politicized. Ackerman agrees with Moe and Caldwell, the politicization of the bureaucracy has its roots in the struggle between the executive and the congress over its control. The difficulties to change legislation contribute to create an autonomous bureaucracy. Again, these are not features of all separation of power systems.

Actually, Ackerman initiate his discussion of this topic noting what is peculiar of the United States scenario:

> At the time they were writing the Constitution in 1787, the Founders did not have the slightest idea that the American government would one day employ millions of officials exercising a bewildering variety of functions" (688).

Hence, a bureaucratic or administrative state was not part of the original Constitutional design. The executive-legislative struggle over the control of the bureaucracy is a consequence of this constitutional silence. Hence, most of the bad characteristics of the American bureaucracy Ackerman attributes to the separation of power systems are, in fact, specific to the US. They follow from the incompleteness of the American constitution. I take this issue in the concluding section.

To sum up, there are few, solid, and consequential outcomes one may derive from the choice of the form of government. The usual arguments found in this extensive literature violate the essence of the neo-institutionalism as a method: behavioral assumptions vary with the institutional set up, so that the divergence in outcomes are not derived from the institutional set up, but from the implicitly assumed variation on behavior. The second usual mistake is to fill *blank spaces* with country specific traits. This is also a problem with institutionalism since it indicates that strategies cannot be derived from macro institutions. There are too many strategies to follow under equilibrium. The result is indeterminacy.

V Presidentialism and Bureaucratic Agencies

Recent scholarly work has emphasized that the American president is much more powerful than the constitutional text indicates (Moe and Howell 1989, Mayer 2000, Mayer 2002, Howell 2003). Political scientists have recently discovered the importance of presidential unilateral power, expressed mainly by the issuing of Executive Orders.

Following the arguments put forth by West and Cooper (1989 581), one may note that a new phase of the presidential power aggrandizement is under way. The authors argue that the recent American administrative process is an arena for competition between the President and Congress. According to these authors view, recent Supreme Court decisions have favored the Executive at the expenses of the Legislative with important "implications both for the character of policy making and for the distribution of power within our political system." West and Cooper argue that a new paradigm of bureaucratic control has emerged, one that "advocates centralized presidential control over the agency policy making while prescribing a passive role for Congress"

West and Cooper (1989 586) relate the emergence of this new paradigm with the characterization of the American political system as fragmented and lacking coordination. In the authors words

> The new model of political oversight has been a natural response to conventional view about the effects of delegated authority. The exercise of broad discretion by administrative agencies has obviously been difficult to reconcile with the tenets of representative democracy and separation of powers. Beyond this, it has been frequently identified as a source of malaise in the policy-making process.

The new paradigm is a response to this malaise, to the

> equation of delegated authority with a fragmented policy-making system that is inherently unaccountable and uncoordinated. The popularity of the prescription for centralized presidential control over the administrative process is quite understandable given the pervasiveness of such indictments.

Hence, as legislative studies made its way to comparative politics, popularizing one particular view of the conventional wisdom, the American political system entered a new phase. A phase in which the balance of power tilted in the presidential direction. To centralize the policy-making process in the presidential hands, since at least the Reagan presidency and the issuing of the Executive Orders 12291 and 12498, is the current trend. The Supreme Court has supported this trend in key decisions. As I noted previously, the president has been the omitted actor in formal models of politics.

That has important consequences for the comparative analysis of separation of power systems. In constitutional terms, American presidents are weak. Presidents, by the very definition of presidential system (see Shugart and Carey 1992), hold legislative powers. The American presidents legislative power is confined to a reactive legislative power. More than that, the American president is confined to the weakest form of veto power: the package veto. Most presidents have active legislative powers, as the exclusive prerogative to initiate legislation in certain areas, control over the introduction and execution of the budget, and last but not least, decree power. Hence, most presidents are powerful than the American.

Hence, Tsebelis (1995 325) is wrong when he asserts that

> In parliamentary systems the executive (government) controls the agenda, and the legislature (parliament) accepts or rejects proposals, while in presidential systems the legislature makes the proposal and the executive (the president) signs or vetoes then.

The relation between Executive and Legislative varies with the legislative powers the Constitution assigns to the president[17]. Few presidents in existing systems cannot initiate legislation. Not only are presidents often endowed with the capacity to initiate legislation; often they also have the exclusive right to initiate legislation in some areas (such as appropriation and budgetary matters), whereas legislators are restricted in their capacity to amend bills in these areas. Hence, contrary to Tsebelis (1995), presidents can do much more than simply sign or veto bills proposed by the legislative.

In addition, some presidents also have decree-power; they are constitutionally able to unilaterally alter the status quo. Even though there is considerable variation in the specifics of presidential decree-power (Carey & Shugart 1998), often presidential decrees enter into effect first (whether immediately or not) and the legislature acts second. The legislature acts a posteriori, rejecting, amending or accepting the new status-quo brought about by the executive decree.[18] Given decree-power, therefore, a president can dictate the legislative agenda by forcing the legislature to make a decision on some matter it could, otherwise, not have appreciated. Thus, no group in the legislature, not even the majority, can "close the gates" for a presidential initiative made by decree.

Note that the power to impose an agenda does not imply that presidents will always prevail against the will of the majority. In fact, as Huber (1996) shows, since a legislative majority can always reject a presidential decree, a model of executive-legislative conflict is unable to explain why the executive would ever make use of decrees. There are, of course, strategic advantages that the agenda setter may explore. But as Krehbiel (1988 270) has argued, these are not properly anti-majoritarian devices.[19]

In addition, the government's legislative and agenda powers, among which decree-power, need not be interpreted as means for solving "vertical" conflicts, that is, conflicts between the government and the opposition. Rather, as argued by Huber (1996), the government's legislative powers are also means for solving "horizontal" conflicts, that is, conflicts between the government and its supporters. In this sense, these are ways that the government has to protect the cohesion of its coalition against the opportunistic behavior of its members.[20]

It follows from this that, because of presidents' legislative powers, separation of powers in presidential regimes is not as complete as it is usually considered to be. Presidential legislative powers are commonly interpreted in the context of the US constitution, that is, as means to create checks and balances. But, as we just have seen, the legislative powers of the executive are not only a mechanism for checking the power of the majority or imposing the will of the president. They are also weapons of the majority. Therefore, the fusion of executive and legislative powers is not absent from presidential systems.

Note that this interpretation is at odds with Shugart & Carey`s (1992) view according to which presidential systems that endow presidents with considerable legislative powers —what they call strong presidents —have greater probability of experimenting a breakdown. They argue that strong presidents will have smaller incentives to negotiate with congress and, thus, paralysis and crisis are more likely. This is so because strong presidents have the institutional means to impose their will on congress; weak presidents, in turn, know that they have no other alternative than to negotiate. This argument, however, is based on the "vertical conflict" model and disregards the possibility that the president will try to organize a majority in congress. But once the possibility that the president and the majority have overlapping preferences is considered, then legislative agenda powers need not imply paralysis, crisis and eventual breakdown.

The organization of congress and the degree of control the executive has over the legislative agenda does influence the behavior of individual legislators. They act in a constrained environment. If they want to influence policy, they have to do so according to the rules of procedure of the body they belong to, and in the terms set by the president. Thus, for example, the incentives to cultivate the personal vote that stem from the electoral arena may be entirely neutralized in the legislature though a distribution of legislative rights that favors the executive. For this reason, we cannot deduce, as it is commonly done, the behavior of legislators from electoral and party legislation alone.

In this context, the case of Brazil is of central theoretical interest for it provides an example of the far reaching effects of the centralization of the decision making process. The system produced by the 1988 constitution is frequently cited as *the* example of bad institutional design (Ames 2001). All of the institutional choices that should not be made, it seems, were made in 1988: a strong presidential regime (one of the strongest in the world according to Shugart & Carey's 1992 155 rank); proportional representation formula for legislative elections with high district magnitude; very permissive party and electoral legislation (e.g., open-list and low party control over access to the ballot). In such a system, the party system is bound to be fragmented and presidents can be virtually certain that their party will not control a majority of seats in both legislative houses. And even if they did, parties would be highly undisciplined thus making the majority status of the president a mere formality (Sartori, 1994 113; Mainwaring 1991). Hence, to have their agenda approved, presidents would use their strong legislative powers, which would lead to conflict and paralysis. To paraphrase Sartori (1997), the system created in 1988 was nothing but hopeless.

Yet, the performance of the post-1988 Brazilian regime is completely at odds with what we would expect to find on the basis of this institutional analysis. Brazilian presidents of this period have had great success enacting their legislative

agenda. Presidents introduced 86% of the bills enacted since 1988 and the rate of approval of the bills introduced by the executive was 78%. Presidents have formed coalitions to govern, and have been able to reliably obtain the support of the parties that belong to the government coalition in approving its legislation: the average discipline of the presidential coalition, defined as the act of voting in accordance with the public recommendation of the government leader in the floor, was 85.6%. This support is sufficient to make a presidential defeat in a roll call a considerably rare event. Thus, despite the "centrifugal" characteristics of Brazilian presidentialism, as indicated by the party and electoral legislation, presidents have been able to govern relying on the support of a disciplined coalition (Figueiredo & Limongi 2000).

This outcome is a result of both the way the Brazilian congress is organized and the president's ability to control the legislative agenda. The Brazilian congress is highly centralized. Legislative rights heavily favor party leaders, who are taken to be perfect agents of their caucuses (*bancadas*) when it comes to most procedural decisions (such as the request for roll-call votes, the closing of debates and, most importantly, the designation of a bill as urgent for purposes of appreciation). The urgency request is a kind of "discharge petition:" it removes the bill from the committee and forces its immediate (24 hours) deliberation by the floor. Bills that are appreciated as urgent cannot be freely amended: only amendments signed by 20% of the lower house are accepted, which implies that only those amendments supported by party leaders will be considered. As Figueiredo & Limongi (2000:157) have shown, the approval of the urgency petition, in turn, is highly associated with the success of a bill. Centralization, thus, deprives members of congress of the legislative rights they need to control in order to influence legislation.

The Brazilian presidents, thanks to their constitutional legislative powers, have a direct influence on the definition of the legislative agenda. Using its decree-power, the executive places on the agenda what it deems to be the most relevant and pressing issues. The president can also influence the pace of ordinary legislation by requesting urgency for the appreciation of specific bills (which will give each house 45 days to deliberate on them). The president has also the exclusive right to initiate legislation related to the definition of the budget, taxation and public administration. Therefore, the executive monopolizes the legislative initiative on the most crucial areas of policy-making.

Hence, it is via the participation in the government that individual legislators will obtain access to resources they need for political survival: policy influence and patronage. Leaders bargain with the executive: they exchange political support (votes) for access to policy influence and patronage. The executive, thus, provides party leaders with the means to punish backbenchers who do not follow the party line: their share of patronage may be denied. The executive, in turn, given the

resources it controls, is in a very advantageous position. Party leaders become, in fact, the main brokers in the bargaining between the executive and the legislators. Contrary to what is currently assumed about Brazil, presidents do not need to bargain on a case-by-case basis. They are in a position to demand support for their entire legislative agenda. Once the government is formed and benefits are distributed among the members of the coalition, the president, with the help of party leaders, may threaten representatives and actually punish those who do not follow the party line. Hence, to say it once more, the actual pattern of legislative-executive relation in Brazil's presidential regime is rather different from what one would expect to find if we were to deduce it from its electoral and partisan legislation.

It should be clear by now that separation of powers does not necessarily imply decentralized decision-making. Institutional analyses that stress the negative effects of separation of powers, and that point to specific, often restrictive, electoral laws as a corrective to these effects, entirely miss the point. Presidentialism does not necessarily imply, or require, decentralized decision-making and conflict between the executive and the legislative. Once one assumes the possibility that coalition governments may also exist in presidential regimes, the degree of overlapping between the executive and legislative majorities has to be adjusted.

Presidential control over the agenda becomes a weapon to be used *by* the majority and not *against* the majority. We can see, thus, that presidents are not necessarily as distinct from prime minister as it is normally assumed. As we showed above, outcomes that are usually associated exclusively with parliamentarism, such as executive success and dominance over the legislative output obtained through disciplined parties, can be found even in "hopeless" presidential regimes such as Brazil's.[21]

Brazil and the United States are both presidential systems. Yet, they are radically different systems. The conventional wisdom in the comparative field, for the reasons I tried to spell out on previous sections, tend to equate both systems. Moreover, comparative institutionalism is badly equipped to understand the role of the president in the Brazilian system.

The Brazilian and the American independent agencies have been created in different contexts. Although discussing the European case, Majone (1997 1) account explains the origins of regulatory agencies in Brazil. According to this author,

> Since the late seventies, European governments have been forced to change their traditional modes of governance in response to such trends as increasing international competition and deepening economic and monetary integration within the European Union. Strategic adaptation to the new realities has resulted in a reduced role for the positive state and a corresponding increase in the role of the regulatory state: rule making instead of taxing and spending.

One just needs to adapt the quotation. First correct the date: the change took place later in Brazil. Mid to late nineties is the correct date. The question then is to explain why Brazil was a latecomer to this process. Second, monetary integration was not related to European Union but it was a factor. What remains to be explained are the consequences of these changes in the mode of governance. This a whole new research agenda that intend to embrace in the near future.

VI Concluding remarks: the limits of institutionalism.

The variables chosen by comparativists are too macro to have such a precise influence over the strategies of all the relevant actors. Institutions do matter. They do constrain the set strategies political actors pursue. But, there are more institutions than forms of the government and electoral laws that do matter. Besides, institutions do interact with one another and there is much that is left to be determined along the way. Besides, we will not be sure that we have specified all the relevant strategies available to the actor. One cannot define these strategies looking exclusively to the form of government. Other institutions, most of them country specific, will also matter. Moreover, path dependence will also play a role since there are different possible answers to non-specified contingencies.

One aspect of these observations, what transaction-cost analysis refers to as the incompleteness of contracts, is of special interest. It questions the basis of institutionalism as a method. Constitutions and statutes, like contracts, cannot specify every possible contingency. Hence, strategies may not be precisely defined ex ante. Avinash Dixit (1998 20) observation is a good point to start:

> If constitutions are contracts, they are very incomplete ones. They do not spell out the rules and procedures to be followed in every conceivable instance in precise detail. They leave much to be interpreted and determined in specific future eventualities

The point is related to Ackerman observation about the American constitution quoted at the end of the fourth section. The American constitution precedes the advent of the administrative state. Besides, as Moe and Howell (1999 850) note

> The Constitution sets out the entire design of American government in just a few brief pages and almost entire lacking in detail. (...) The actual power of the three branches, then, both in absolute sense and relative to one another, cannot be determined from the Constitution alone. They must of necessity, be determined in the ongoing practices of politics. And this ensures that the branches will do more than struggle over day-to-day policy making. They will also engage in a higher order struggle over the allocation of power and the practical rights to exercise it.

Hence, the different branches of the government fight to control what contract analysis calls the residual power. Each branch fights to incorporate as its duty what is left ambiguous by the Constitutional text. Note that a successful claim over the non-specified part of the institutional contract may lead to a new layer of institutional power. A successful claim over the residuum may lead to its institutionalization.

Of course, this is not true only for the American constitution. This happens everywhere. Bagehot's account of the English constitution, of its transformation, is an assessment of how profound such changes may be.

Clearly, this defies comparative analysis based upon macro variables as form of the government, electoral laws and so on so forth. Within each of these groups, there may be too much variation. It follows that one may not be able to specify common strategies and, thus, derive outcomes. In these terms, institutionalism as a method may be condemned to failure.

NOTES

1 Basically, that all actors have single peaked preferences. Note that this is not an assumption about individuals, but about the collectivity given individual preferences must be related in a precise way.

2 I intend to develop this section. I want to discuss that for noncooperative game theory, one does not simply aggregate preferences. Beliefs about strategies are endogenously generated. Hence, there is space for deliberation in game theoretic models. Besides, recent developments in economy theory, the so called transaction costs analysis, indicates that contracts cannot specify all contingencies. That limits the reach of institutionalism as a methodology.

3 See Ferejohn 1986 for thoughtful discussion of the complexities involved. Shepsle and Weingast (1987) failed in their attempt to model "the institutional foundations of the committee power". The proposed model has noncooperative tone but it did not survive Krehbiel's (1987) criticism.

4 I will cite the omitted passage below.

5 In this account, policies are not set by special interests either. Hence this view differs from the one proposed by the Chicago School. The latter is a capture explanation: capture of the agencies by the special interests. The regulated industries use the power of the state to extract benefits. As Moe notes, the Chicago School does not model institutions. They are incorporated as black boxes to indicate that they do not matter. The bureaucracy also does not play any real role either.

6 I can't find where.

7 This is the omitted part in the quoted passage above.

8 This is the case of Becker (1983). He argues that voters face high costs to get political information. These costs exceed the returns they can obtain via their vote. Thus, it is rational to be politically ignorant.

9 This section relies on Cheibub and Limongi 2002.

10 See Strom (1990:8-9) for a summary of findings. See also Laver and Schofield (1998:70) and Cheibub (1988).

11 See also Laver and Schofield (1998) for a discussion of minority governments in European parliamentary regimes and for an argument for the inappropriateness of the "majoritarian imperative" for the analysis of these systems.

12 These numbers are drawn from Cheibub 1988.

13 The factors that led to this transformation are complex and are beyond the scope of this paper. It is sufficient to say here that a central factor is the fragmentation of the party system that resulted from the December 1973 election. In that election, the four traditional parties that had dominated Danish politics since the early 1900s (Conservatives, Liberals, Radical Liberals and Social Democrats) obtained about 60% of the seats, down from over 90% in the previous parliament. Three parties obtained representation for the first time (Progress Party, Christian People's Party, and Center Democrats), and two parties (Communists and the Justice Party) obtained seats for the first time since 1957. Overall, the new parliament had 10 parties, twice as many as it had prior to the elections. The pattern of government formation that resulted was also different. Whereas no single party majority government has ever been formed since 1945, prior to 1973 half of the governments were single party minority governments, and another 40% were majority coalition governments. After 1973, however, no majority government has been formed and 55% of the governments were coalition governments.

14 The electoral reform approved prior to the June 18, 1989 election, the first in the series of three, did make the government formation process more complex by increasing the degree of proportionality in the system and thus favoring smaller parties. According to analysts, this reform "was widely seen as designed to reduce the likelihood of New Democracy forming a one-party government after the June election" (Keesing Contemporary Archives, on-line, volume 35, March 1989).

15 Governments are marked by the change of the President, by the change in the partisan composition of the government, or by changes in the share of seats held by governments parties in congress due to legislative elections. We find that the third criterion is problematic since it implies that no government survives a legislative election. Unfortunately it is not possible to distinguish from the published numbers by how much this inflates the counting.

16 Studies of coalition government under presidentialism are still few. Other references include Amorin Neto (1998), Foweraker (1998) and Altman-Olin (1999).

17 This and the next paragraphs rely heavily on Cheibub and Limongi 2002.

18 Note that often rejection of a presidential decree does not mean a return to the status quo ante. Even if there is a majority in favor of the status quo, once the decree has been in effect, rejecting it may have become an unattractive or unavailable alternative.

19 It is true that, since it immediately alters the status quo, the decree power will increase the power of the agenda setter. When legislatures have to vote on ordinary propositions, legislators compare the status quo (SQ) with the situation to be created by the proposition. In the case of an executive decree, the legislator compares the situation created by the decree (D) with the new situation created by rejecting a decree that has been in effect for some time (SQD). If the preferences of the majority are SQ>D>SQD, then *the majority* will approve the decree. If the preferences of the majority are SQD>D (assuming that SQ is no longer a viable alternative), then *the majority* will reject the decree.

20 It is interesting to note here that there seems to be no association between minority status and the use of decree-power (Figueiredo & Limongi 1998).

21 Now, if presidential regimes are not all alike, neither are parliamentary systems. That the government will control the legislative agenda does not follow from the definition of parliamentarism. Neither is it necessary that the

legislative rights of private members be curtailed in parliamentary regimes. Committees may have considerable powers in parliamentary assemblies and may erect barriers to the executive agenda.

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Fernando Limongi

PROFESSOR OF POLITICAL SCIENCE AT UNIVERSITY OF SÃO PAULO - USP

PRESIDENT OF BRAZILIAN CENTER OF ANALYSIS AND PLANNING - CEBRAP

NEW PUBLIC SPHERES IN BRAZIL: LOCAL DEMOCRACY AND DELIBERATIVE POLITICS

Leonardo Avritzer

Brazil is one of the countries in which a very large number of participatory experiences emerged in the last ten years. These experiences are related to two transformations in the country political landscape: the first transformation was the change in associative pattern which was part of the process of democratization and took place between the late seventies and mid-eighties. Neighborhood associations blossomed in this period as part of a general associative movement in reaction to authoritarianism. In Rio de Janeiro, more associations were formed between 1979 and 1981 than in the whole previous democratic period (1946-1964). In Belo Horizonte, 80% of the existing neighborhood associations date from the 80's (Avritzer, 2000). In Porto Alegre, a city whose associative tradition goes back to the fifties, this was a moment in which community associations claimed participation in the elaboration of the city budget.

The second important transformation in democratic Brazil was the emergence of participatory and deliberative legislation at the end of the Constitution making process. The Brazilian constitution increased the forms and the arenas of participation. In its article 14, the Constitution acknowledged that popular sovereignty could be exercised through the vote but also through popular initiative. In its article 26, on the cities, the constitution required the participation of representatives association in city policies. In its articles on health and social security (articles 204, 227), the Constitution required the participation of the population in the formulation and control of these policies. The legal infra-structure for participation was in place in Brazil in the late eighties. Yet, very few mayors or political parties took advantage of

it as well as the Porto Alegre administration, which introduced a practice called participatory budgeting when Olívio Dutra was elected mayor of Porto Alegre in 1988.

Participatory budgeting is a local practice of public deliberation on budget issues introduced in Porto Alegre in 1989 and which is today practiced in 103 Brazilian cities. It is characterized by four elements: the first one is the delegation of sovereignty by elected mayors to a set of regional and thematic assemblies which operate through universal criteria of participation. Every citizen can participate and vote on budget issues in regional and thematic assemblies. The second characteristic is the combination within the participatory model of different elements of participation which belong to different participatory traditions, such as direct participation and election of councilors at the city level. The third element is the principle of self-regulation. The rules for participation and deliberation are defined by the participants themselves and are adapted or changed every year(Santos and Avritzer, 2002). The fourth element is an attempt of inverting priorities in the distribution of public goods through a combination of participation and technical decisions on whom should have access to public goods. How this formula of public deliberation emerged? Is it specific to the political configuration of the city of Porto Alegre? Can it be extended to other parts of Brazil and democratize the country's political culture?

This article is going to approach the transformations in the Brazilian political landscape that led in the first place to the emergence of participatory budgeting in Porto Alegre. In its first part, we will discuss the emergence of the experience and engage in the debate on its exceptionality. The Southern region of Brazil has always had a more participatory culture than other parts of the country. In the first section of this paper, we will show what are its main elements and will relate them to emergence of participatory budgeting. In this article second part, I will analyze two experiences of PB, Porto Alegre and Belo Horizonte and I will approach its deliberative and distributive elements. I will show the level of deliberative equality involved in the PB. I will also discuss a still existing deliberative gap between those who participate and those who speak. In this paper third part, I will analyze the recent extension of participatory budgeting experience, pointing out the variations they involve and comparing the levels of participation and the changes in democratic culture in each case.

The Emergence of Participatory budgeting: an explanation

The state of Rio Grande do Sul where the city of Porto Alegre is located tried hard during the nineteenth century to separate itself from Brazil.[1] Its process of political formation involved several different characteristics than those that prevailed in Brazil as a whole: slavery played a central role in the Brazilian process of nation-building

and, yet, it was not very strong in the South of Brazil, where most cases of slavery were cases of domestic slavery (Conrad, 1993). In addition to that, some of the institutions which were central in the Brazilian nineteenth century such as the guarda nacional, which was the transformation of great landowners into colonels of the national guard were not accepted in Rio Grande do Sul. There, civic militias functioned regularly between 1835 and 1845 leading to a less hierarchical culture and the emergence of the idea of social honor (Uricochea,1984). Big rural property was another important characteristic of the Brazilian process of nation-building (Furtado,1963) which has never been important in the Northern part of the state of Rio Grande do Sul in which small property and an urban network of small rural cities contributed to a more egalitarian sociability (Baquero,1995:20). In addition to that Rio Grande do Sul received more than its fair share of Brazilian immigrants in the late nineteenth and early twentieth century. Thus, throughout the process of nation-building in Brazil during the nineteenth century, Rio Grande do Sul was an exception in term of its main structural characteristics.

The origin of popular movements in Porto Alegre in the post-war period is marked by the formation of Fracab, Federation of Community Associations in Rio Grande do Sul, created in the second half of the 50's (Silva,2001:79). From its very origin, the community movement in Porto Alegre could be differentiated from those of other Brazilian cities. In the case of São Paulo, the Sab's – Society of Neighborhood Friends, had a predominantly recreation nature (Gohn,1991). In the case of Belo Horizonte, there has been very little community mobilization and association in the same period. The city whose associative dynamics seems to be similar to Porto Alegre is Rio de Janeiro, which also had a strong associative movement in the post-war period (Boschi,1987). Thus, we have a first moment of differentiation between Porto Alegre and other Brazilian cities in the organization of community movements which created an associative drive still in the fifties.

When the new associative drive begins in Brazil in the late seventies (Santos, 1993), the pattern of association changes in most Brazilian cities. In the cases of Belo Horizonte and Recife the number of community associations tripled in the eighties (Avritzer, 2000; Silva, 2002). In Rio de Janeiro there was a huge associative drive between 1979 and 1981. In São Paulo there was a huge change in the aims of community associations which became more politicized in this period. In the case of Porto Alegre, since the 60's, there was in the city a tradition of a claiming for community improvement in a more organized way, due to the creation of The Liga Interbairros Reivindicatória e Acessoradora (Intercommunity League), an umbrella association which included among its aims the idea of an "humanist, antipaternalist" form of participation. (Silva, 2001:81). The existing tradition of associations evolved in the eighties in Porto Alegre to a new umbrella association, UAMPA, which claimed for the first time the right to participate in the deliberation on budget issues

at the local level in 1986 (Uampa, 1986; Avritzer, 2002c). Thus, there is in the case of Porto Alegre a tradition of community mobilization that differentiated it from other Brazilian cities, from the fifties through the eighties.

Porto Alegre also had a tradition of more left wing political behavior. This tradition can also be traced back to the post-war period. Between 1947 and 1963, the PTB (Brazilian Labor Party) was the party which received the largest share of the votes in the elections for city Council. The candidate of the PTB for governor won all the elections in the city of Porto Alegre between 1947 and 1964 (Silva,2001). In the moment in which redemocratization took place in Brazil (1985-1988), there was a dispute between left wing and right wing candidates in most Brazilian capitals with the exception of Porto Alegre. There the dispute was between the PDT, a center left party which seek to retrieve the populist past and the PT, the Workers Party, a party which seek to renew the Brazilian left and proposed popular councils as a form of governing the cities (Keck, 1992; Abers,1996). In the first round of this dispute, the PDT won the first elections for mayor after redemocratization and tried to introduce participatory policies. At the same time, community associations and the PT claimed that the forms of participation were too limited. It was in this context that UAMPA launched the idea of participation in the budget making process. Thus, it is possible to argue that Porto Alegre was the only city in Brazil in which the political dispute in the aftermath of redemocratization took place among sectors of the left and was centered on the issue of participatory policies at the local level.

It was in this context that Olívio Dutra was elected mayor of Porto Alegre, in 1988, and introduced participatory budgeting as the policy for deliberation on the distribution of public goods by his administration. Participatory budgeting emergence is the result of structural characteristics present only in Rio Grande do Sul at that point, such as the way these structural characteristics generated a strong community movement in Porto Alegre, the arrival of the PT to an administrative position in the city, the new legal infra-structure of participation generated by the 1988 Constitution and the claim for participation which emerged in the first 30 days of Olivio Dutra's administration.

The initial design of participatory budgeting did not follow the will of any of these authors. On the contrary, it was the combination of a proposal for participation made by each one of them. Uampa, the Umbrella organization for community associations in Porto Alegre, centered its proposal of participation in regional assemblies with a strong organizational twist, in which members of neighborhood association would decide on budget issues. The PT proposed the creation of popular councils at the local level, in which members of a city council would be elected. Against UAMPA, and following the logic of local politics, the administration proposed that participation in the PB should be individual instead of by entities.[2] However, the administration accepted UAMPA's proposal that participation should

take place at the local level in a series of regional assemblies which should follow the logic of popular mobilization in the city. In the second place, the local PT insisted in a constitution of a council which was, at that time, part of the conception of the need of a parallel form of power. (Abers,1996). It was from this conception that the COP , Council of Participatory Budgeting emerged. Yet, the role played by the COP in the formation of an institutional coordination of the proposals emerging at the local assemblies was completely new. Last but not least, the administration itself perceived that it would have to change its functioning in order to allow for participatory budgeting to work. It completely changed the format of the CRC and at the same time created a new institution, the GAPLAN, Planing Cabinet, which would be in charge of elaborating the budget under the supervision of both the Participatory Budgeting Council and the mayor cabinet. Table 1 below synthesizes each of the main actors which made a proposal for the institutional organization of the PB and the format it acquired in the early nineties.

TABLE 1

	ORIGINAL PROPOSAL FOR PARTICIPATION	FINAL DESIGN
NEIGHBORHOOD ASSOCIATIONS	DIRECT DELIBERATION AT THE LOCAL LEVEL. PARTICIPATION OF MEMBERS OF COMMUNITY ASSOCIATIONS.	REGIONAL ASSEMBLIES WITH INDIVIDUAL PARTICIPATION
LEGAL INFRASTRUCTURE	CONSTITUENT ASSEMBLY INTRODUCES CITIZEN PARTICIPATION AS A PRINCIPLE	PORTO ALEGRE CHARTER ADOPTS PARTICIPATION AS ITS FIRST PRINCIPLE
WORKERS PARTY (PT)	POPULAR COUNCIL AT THE CITY LEVEL	REGIONAL AND THEMATIC ASSEMBLIES ELECT COUNCILORS FOR A COORDINATING BODY.
LOCAL ADMINISTRATION	CONCENTRATION OF CLAIMS ON THE CRC	CRC BECOMES PART OF PARTICIPATORY BUDGETING STRUCTURE

Thus, participatory budgeting is the result of the Brazilian process of democratization as well of its impact in the country's region which developed the most democratic tradition. It took advantage of the new legislation which emerged in the Constitution-making process as well as of the productive overlapping of a tradition of democratic associations in the South with a specific proposal for participation which emerged within emerged in the Workers Party.

Today, 103 cities in Brazil practice some form of participatory budgeting, among them, São Paulo, Belo Horizonte, Recife and Porto Alegre, 4 among Brazil's five largest cities.(Teixeira,2003). Among all these cases, I will like to single out a second case for comparison with Porto Alegre, the case of Belo Horizonte. Belo Horizonte is Brazil's third largest city with a population of a littler more than 2 million inhabitants. Its political formation is very different from Porto Alegre. Belo Horizonte is located in the more conservative state of Minas Gerais and is a city founded in 1897. The associative tradition is the city was very low during most of the 20th century. In the first 80 years of existence, only 70 neighborhood associations were formed in the city. This tradition changed with the associative drive of the democratization. The number of neighborhood association in the city increased from 70 to 534 between the mid-seventies and the mid-eighties (Avritzer,2000). Politically, Belo Horizonte has always been more conservative than Porto Alegre. It was home to the so-called "Minas oligarchy" a group of conservative politicians who played an important role in the post-war democratic period (1946-1964) and who generated the leadership of the conservative path of transition to democracy in 1985. Yet, the Workers Party (PT) has also been strong in Belo Horizonte since its formation and eventually won the elections for mayor in 1992 when it also proposed to introduce participatory budgeting in the city. Today, the PB has been practiced in Belo Horizonte for 10 years. In the next session of this paper, I will analyze briefly and describe participatory budgeting in the two cities and I will analyze its distributive and deliberative elements. In this paper concluding remarks I will analyze participatory budgeting in a comparative perspective.

Participatory budgeting: an analysis of its deliberative elements

Participatory budgeting changed the process of budgeting-making in Brazil. In its most important experience in Porto Alegre (1990-2003) it introduced 4 new types of institutions, three of which show the presence of deliberative elements, namely the regional and thematic assemblies, the Council of Participatory Budgeting, COP, and the form of decision on the rules for decision-making.[3] The regional and thematic assemblies are places where participants make their claims, criticize the local authorities in relation to previous administrative actions and also negotiate among themselves on which are their priorities. There are in Porto Alegre 16 regions (see map 1) and five thematic assemblies. The format of the regions was a point of conflict between social movements and the administration. Social movements pressed hard for the maintenance of a collective action logic in the regionalization of the city, arguing that the administrative zoning would collide with the mobilization logic of many community movements (Baierle, 1998). The city of Porto Alegre agreed to redesign the regions adopting an administrative logic which overlapped with the

existing forms of mobilization. Thus, the first element in the deliberative process was an attempt to combine a collective action logic with an administrative logic.

Regional and thematic assemblies are places for discussion and deliberation. An analysis of the socioeconomic characteristics of the participants show a strong presence of poor urban dwellers in the regional assemblies. 30,22% among them make up to two minimum wages, 25,51% make between 2 and 4 minimum wages, showing that the level of participation in the PB is very close to the socio-economic condition of the population. In each of these assemblies, 45 minutes, are open for the manifestation of the participants. The presence in the assemblies does not fully translate itself in equality in other levels, when we make move our analysis from presence in the assemblies to expression in the same assemblies. Table 2 below shows selected data on gender and socio-economic condition of those registered to speak in assemblies in the PB in Porto Alegre.

TABLE 2

Socio-economic condition of the participants and of the speakers in the assemblies in POA

SOCIO-ECONOMIC LEVEL	PARTICIPANTS IN THE ASSEMBLIES	NEVER SPOKE IN THE ASSEMBLIES
UP TO 2 MINIMUM WAGES	30,22%	47,30%
2 TO 4 MINIMUM WAGES	25,51%	37,90%
4 TO 8 MINIMUM WAGES	20,60%	37,20%
8 TO 12 MINIMUM WAGES	———	27,10%

Source: Cidade

Thus, it is possible to note several deliberative characteristics of the regional assemblies of the PB in Porto Alegre: in the first place they are able to express the social diversity of the city, of its different social components, a characteristic that, as we are going to show below, will determine a new social balance in the process of deliberation on the distribution of public goods. In the second place, though there are still some inequalities in relation to gender participation or social participation, it is interesting to point out a certain equilibrium in the gender relation in the number of interventions. Participation of women in the PB meeting is higher than participation of men (51,4% of the participants are women) and higher participation also expresses higher willingness of speak. Yet, we can note that socio-economic conditions predetermines sharply the ability to speak. Among the participants that make up to two minimum wages and are the majority of the participants, 47,30% among them never spoke in na assembly. The number of people who never spoke decreases in an unverse

proportion to their socioeconomic characteristics. In the next session of this paper I will show that the presence and expression capacity of women and the poor has consequences in the profile of the public goods distributed in the regions.

A second deliberative body of the PB is the COP, the Council of Participatory Budgeting. The COP is formed by in the second round of regional assemblies, when the region elects councilors to the PB council. This process leads to the formation of a council composed as follows: two councilors from each of the 16 regions (32), two from each of the five thematic assemblies (10), one from the Uampa – the umbrella organization of neighborhood communities – and one from the public service trade union (2). The PB council thus has 44 members. Administration members do not have voting prerogatives at the PB council though they participate regularly and have a strong influence.[4] The PB Council can be considered a deliberative body in which two types of negotiations take place: the negotiations between community members on their priorities and the negotiation between community members and the administration on the final format of the budget. Several decisions take place at this level such as: the substitution of previous decisions due to technical reasons. Technical reasons in the PB jargon is a veto imposed by the technical members of the administration on deliberations of the regional assemblies. These most common vetoes involve environmental issues, property issues and financial issues. Environmental vetoes that are common in Porto Alegre involve the extension of the process of channeling local creeks[5], which is demanded by the population and considered by the city technicians a cause of summer floodings; property issues involve mistakes in the identification of the owners of land which is considered city land and turns out to be owned by state companies or the state or the union; financial issues involve technical considerations on the cost of extending sewage or water pipelines to areas that they have not yet been reached by them. In all these cases, there is a strong debate between the members of the PB Council and the administration with mixed results. One of the important results of these debates is the requirement imposed by the administration that the technicians attend the regional and thematic assemblies and discuss their positions on these issues with the population. Again, it is important to note that the presence eof the technicians in popular assemblies increase their deliberative nature.

The third deliberative element of the PB is the process of decision-making on rules for deliberation. Porto Alegre inaugurated an understanding on the process of making rules for deliberation that so far has been followed by other cities in Brazil. According to this process, the city determined the initial rules for deliberation (regimento) and the PB Council acquired the prerogative to change it from the second year on. These rules involve: the composition of the Council of the PB (COP); the attributions of the Cop; rules for the election of delegates at the local level; conditions upon which a mandate could be lost; the rules for argumentation in the COP; rules for the election of a coordination body within the COP and, last but not least,

rules for the COP to change on a yearly basis the rules for deliberation (regimento). Thus, the COP may be understood as a body which sets up its own forms of regulation, from composition to rules for deliberation. It shares some of its prerogatives with other bodies, such as the CRC and the GAPLAN. However, the final deliberative process on budget making takes place at the COP level and implies in a process of making rules for deliberation which is the attribution of the COP itself.

The organization of the PB in Belo Horizonte is different from Porto Alegre. The PB has been in practice in Belo Horizonte since 1993. It involves two rounds of regional assemblies which lead to a regional forum of priorities. In the first round, the administration points out the resources available for public works in the areas of pavement, sewage, and housing. The decision-making process is also different from that used in Porto Alegre. The administration announces the resources available for each region based on a index called IQVU, Index for Urban Quality of Living. 50% of the PB's resources are evenly divided among the regions and 50% are allocated according to this index. Also in the second round, the main proposals for public works in each sub-region (Belo Horizonte has 37 sub-regions, see Map 2) are presented, initiating a process of negotiation among the communities.

The second round of regional assemblies is the most deliberative moment in Belo Horizonte's PB. It involves the election of delegates who will vote on the public works to be included in the city budget. Delegates were elected in 2002 according to the following criteria: from 1 to 200 participants, one delegate for every 10 people attending the assembly; from 201 to 410 participants, one for every 15; above 410, one for every 20. In addition, each region is entitled to one delegate per legally constituted voluntary association within its boundaries (BH, 2002). Once the delegates are elected for the forum on regional priorities, negotiation begins. The main stage in the negotiation process is represented by the "priorities caravans". In this stage, each community which has proposed a public work to be included in the city budget visits other communities in order to evaluate their level of need. At the same time, different communities start to support one another's claims, forming coalitions which will be decisive in the deliberative process.

The final stage in Belo Horizonte's PB, involves a forum of regional priorities. In this forum, there is the formation of tickets with coalitions of proposals from different sub-regions. The ticket are voted with the proposals from each region and unlike Porto Alegre, the decisions of the regional fora are final. The public works approved by the delegates will be integrated into the budget proposal. 20% of the delegates present at the regional fora become members of the *Comforças,* a monitoring body which follows the process of bidding for public works and can negotiate substitutions in case of technical problems.

If we compare the deliberative aspects of the two experiences we can note the following characteristics: first of all, Porto Alegre has more deliberative elements

expressed in the the way the deliberative nature of the assemblies is connected with the Council of Particpatory Budgeting. Belo Horizonte has deliberative elements, expressed in the first and second rounds of assemblies. The assemblies in Belo Horizonte are more connected to a voting process than to a process of argumentation and decision-making. The main difference between the two experiences is the lack of council in Belo Horizonte until 1999. In that year, a council with limited prerrogatives was created. Yet, it has never been truly connected with the deliberative and decision-making process. In the next session of this paper I will discuss how the differences in deliberation are connected with the differences in the design of the deliberative process.

Participatory budgeting: an analysis of its democratic and distributive impact

An issue that has concerned the analysts of participatory budgeting is how to evaluate a deliberative experiment. The levels of participation in the PB are high and increase on a yearly basis. This is true for Porto Alegre the city that inaugurated the practice. This is also true for Belo Horizonte, the largest city which decided to follow Porto Alegre's lead. Finally, this has also been true for São Paulo, Brazil largest city whose PB is in its second year. Table 3 shows levels of participation for the three cities in selected years.

Table 3
Participation in the PB over time

	PORTO ALEGRE	BELO HORIZONTE	SÃO PAULO
FIRST YEAR OF PB	976	15.216	30.000
SECOND YEAR OF PB	3.694	25.580	50.000
FIFTH YEAR OF PB	9.638	21.175	
TENTH YEAR OF PB	13.687		

Source: planning secretaries of the cities

The data show important increases in participation in the cities that introduce PB. Some characteristics of participation in the PB should be stressed. First of all, initial participation in Porto Alegre's PB was low; in the first year, it was low in most regions and very low in those without any previous tradition of social organization, such as Restinga, Glória, Ilhas and Humaitá (where only 36, 20, 80, 10 people respectively participated in the second round of regional assemblies) (Avritzer and Wampler 2003). The

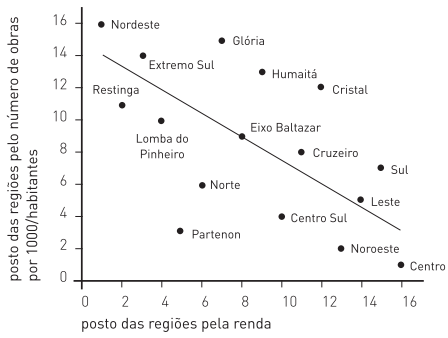
low levels of participation in almost all regions was probably linked to doubts about the capacity of the process to deliver public goods. Beginning in the second year, however, there was a huge change in the pattern of participation. On the one hand, the effectiveness of the first year's deliberations was a strong incentive in those regions which already had a tradition of community organization such as the Leste (east region), where 705 attended the second regional assembly, or Parthenon, where 264 people attended the second regional assembly. On the other hand, participation remained very low in regions without a tradition of participation or community organization. These regions, which are among the poorest, had low levels of political participation for some years. At this stage, the determination of the administration to continue with the participatory process and to implement decisions taken by very few people contributed to increase participation in the following years. Thus, the effectiveness of the deliberative process is essential to increase levels of participation. A second element worth noting is how participation is directly linked to deliberation. The most important aspect of the participatory process in Porto Alegre is the continuous increase in participation in spite of the fact that the fora in which participation has been high have changed. Participation increased from year to year with very few exceptions (1994 and 1996). The continuous increase in participation can be attributed to the confidence that the deliberative process would continue due to the political hegemony of the Workers Party in the city.

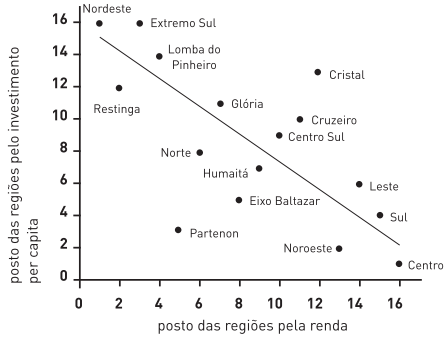
Participation in Belo Horizonte shows more variation due to stronger doubts about the continuation of the process. In the first year, participation in Belo Horizonte was already high due to the demonstration effect of the Porto Alegre experience – the population had good reason to assume that it was participating in an effective process. Participation increased still more once the effectiveness of the process at the city level became clear. In its second year of the PB, participation grew more than 50% over the previous year, but then decreased in 1996 with the emergence of doubts regarding the PB's future. In that year's city elections, there were serious doubts that the Workers Party candidate would win and, thus, that the PB's decisions would be implemented. Participation decreased again in 1997 because, despite the fact that the new, non-Workers Party administration promised to continue the PB process, social actors doubted that it would implement the decisions. However, once it become clear that it would respect the deliberations, participation grew again. Thus, one can argue that participation in the PB varies according to two factors: previous traditions of association and the perceived effectiveness of the process. It is still early to evaluate the process in São Paulo, but it is already clear that participation increased sharply in the second year of PB.

Participation in large cities, such as Porto Alegre, São Paulo and Belo Horizonte, reach the level of 1 to 1,5% of the city population. A few data are more meaningful and involve who participates, how participation of the poor evolves; what is the relationship between participation and abiding to new democratic rules and what is the

relation between participation and distribution. Participatory budgeting in Porto Alegre and Belo Horizonte involve the participation of the average citizen in terms of income levels. Most of the participants in the experiment make in between 2 and 5 minimum wages, an amount which is close to the cities average income level (Avritzer, 2000c). The explanation for the high levels of participation of the poor is that the PB resembles practices already existent at the level of civil associations, such as the regional assemblies. Thus, a previous knowledge on how to participate is already available. At the same time, middle class sectors have not been as active as the poor in community associations in Brazil. Thus, participation of the poor in the PB is high for three reasons: because they have a previous tradition of participation in community issues; because they know how to assure their presence in the regional and thematic assemblies and last but not least because the assemblies of the PB resemble a form of participation in which the poor use to have a stronger presence than middle class sectors.

The participation of the poor is a little lower in the deliberative bodies constituted by the PB such as the Council of Participatory Budgeting or the delegates bodies. If we measure the income and education levels for the members of the PB Council in Porto Alegre and São Paulo (Belo Horizonte does not have a council) we can see that they do not resemble the average income and education levels of the population. In the case of Porto Alegre, 28,2% members of the PB Council make between 4 and 8 minimum wages, an amount similar to the one made by São Paulo councilors. However, if we cross the city investment plan with income levels we can note that the majority of the deliberations benefit the poor. Graphics 1 and 2, reproduced from Marquetti 2003, show the relationship between income and deliberations in Porto Alegre. It is possible to point out a strong correlation between investment levels and low income levels. This correlation has strong deliberative consequences. They show that, the presence of the population in the regional and thematic meetings in Porto Alegre imply in deliberations which affect them positively. Yet, in spite of the distributive effects, it is possible to argue that public deliberation has the strongest consequences at the level of political practices.





The analysis of the distributive elements of the PB in Belo Horizonte also shows strong distributive effects. Macedo (2002), using the IQVU (Index for Urban Quality of Living) showed that Belo Horizonte's PB also has strong distributive elements. Macedo differentiated six classes of UP (panning unities) according to their IQVU and connected the investments of Belo Horizonte's PB according to this ranking. He then showed that PB investments are concentrated in the areas whose IQVU's rank lower (see table 4 below). He also showed that the amount of investment as well as the average number of investments vary according to this ranking.

TABLE 4
Distributive effects of Belo Horizonte's PB

UP ACCORDING TO THEIR IQVU	NUMBER OF UP'S	IQVU GAPS	AVERAGE POPULATION OF THE UP'S	AVERAGE INVESTMENT PER UP (BRAZILIAN REAIS)	AVERAGE NUMBER OF PUBLIC WORKS IN THE PB PER REGION
CLASS I	6	0570-0645	18.677	93.374,20	0,50
CLASS II	19	0491-0550	24.985	307.255,16	0,84
CLASS III	12	0463-0488	35.027	1.185.151,05	2,08
CLASS IV	18	0423-0456	30.102	1.075.192,75	2,44
CLASS V	15	0384-0415	26.109	1.149.208,66	1,73
CLASS VI	11	0328-0368	13.709	1.221.302,76	1,82

Source: Macedo, 2002

Thus, the two cases that we are analyzing show a strong distributive impact. Yet, what is the deliberative impact of the PB and its impact in the democratic culture?

In a survey applied in PB participants in Porto Alegre and Belo Horizonte in 1999[6], we tried to find out the cultural impact of the institutions for public deliberation created in both cities. We first asked whether these actors and their communities could get material benefits from previous administrations and whether they could get material benefits from the PB (see table 4 below). Though, it is possible to see that there is an increase in the amount of communities which got material benefits, we can note that this variation is less significant than the one measured

by a second question on changes in political culture. The second question we asked was about the role of political mediators in Brazil. As it is well known (Grahan,1990; Gay,1984) clientelism plays a strong role in Brazilian cities, and politicians mediate the process of having access of public goods at the urban level. Community associations challenged this practice in Brazil during the process of democratization and brought to the PB this critique. The second issue we wanted to find out in the research in Belo Horizonte and Porto Alegre is whether the deliberative process established a new pattern of interaction between participants and the administration or whether the PB overlapped with other forms of political interaction, in particular with clientelism. Thus, we asked a second question on the influence of political mediators in the process of having access to public goods through the PB. Table 6 below shows the results to these questions. The results show that the PB although the access of the poor to public goods increase that the PB has a largest impact in changing the political culture and establishing a new pattern of interaction at the political level.

TABLE 5
The role of political mediators before and after the PB

	PORTO ALEGRE		**BELO HORIZONTE**	
DID THE COMMUNITY HAVE ACCESS TO PUBLIC GOODS BEFORE THE PB?	YES 62,7%	NO 37,3%	YES 49,3%	NO 49,3%
HOW DID THE COMMUNITY GET PUBLIC GOODS BEFORE DE PB?	THROUGH SOCIAL MOBILIZATION 54%	THROUGH POLITICAL MEDIATORS 41%	THROUGH SOCIAL MOBILIZATION 34%	THROUGH POLITICAL MEDIATORS 60%
DID THE COMMUNITY GET PUBLIC GOODS THROUGH THE PB?	YES 89,6%	NO 11,4%	YES 60,3%	NO 39,7%
WAS IT NECESSARY SOME KIND OF INTERVENTION OUTSIDE THE DELIBERATIONS OF THE PB?	YES 28%	NO 72%	YES 32,9%	NO 67,1%
WAS THE INTERVENTION OF POLITICIANS NECESSARY?	YES 0%	NO 100%	YES 7,3%	NO 92,7%

Thus, it is possible to point out four elements of the deliberative process in Porto Alegre and Belo Horizonte:

1. first of all, the presence of a previous tradition of association influences the deliberation in the moment of the emergence of a participatory process. The data for Porto Alegre show that the emergence of the PB is related to the kind of community associationism which existed in the city. It is true that an associative tradition alone could not generate the PB. Yet, the initiative of the proposal and the fact that it drew on pre-existing practices which emerged at the level of community associations was important for its success. Regional and thematic assemblies are a new important way of claiming for public goods without the interference of political mediators. They establish argumentation and negotiation as a new pattern for the actions of the community and the relationship between the community and public administration.

2. the deliberative process has strong rational characteristics that can be showed by the data on participation in Porto Alegre and Belo Horizonte. The rationality of participation and deliberation in Porto Alegre is what explains the change in the most important institutions in which the population participated. The change in the deliberative process also changed participation. The data on Belo Horizonte are even more convincing. The variations in the level of participation can be attributed to variations in the effectiveness of the process.

3. There is a correlation between participation in the deliberative process and distribution. This correlation has two different dimensions. The first one is the strong presence of the average poor citizen in the PB regional and thematic assemblies. This is true in all cases of PB in large Brazilian cities, though, as I have pointed out above, in the higher decision-making bodies the presence of the poor is lower. Yet, there is a strong correlation between participation and results, a correlation showed by the distributive impact of the deliberations. As, we have showed above the average poor citizen is the final beneficiary of the public works.

4. The deliberative process has a democratizing effect on the political culture. The last important issue is the impact of PB institutions in the creation of a more democratic culture. Table 4 shows that the largest change produced by the PB is not the new access to public goods. This access somehow existed in cities such as Porto Alegre and Belo Horizonte before the PB was introduced. The most significative change is how the access is negotiated among social actors and politicians. We showed that the institutions created by the PB establish a pattern of negotiation which renews the political culture by putting aside political mediators specialized in exchanging favor for material benefits, one of the central dimension of clientelism in Brazil (Leal, 1946).

Thus, it is possible to argue that the new associative culture that emerged in Brazil in the late seventies at the community level, connected itself with a sector of Brazilian political society to create more democratic and deliberative forms of decision making. These forms, which are very important in large cities, such as Porto Alegre, Belo Horizonte and São Paulo have an important impact on the pattern of distribution of public goods as well as in the democratization of political culture. The question that

has to be posed is: can this new pattern be extended to the rest of the country, regardless of scale, regional political culture and city size?

The extension of the PB in Brazil

Participatory budgeting has been extended to 103 cities in Brazil in the year 2000. Contrary to common knowledge, the characteristics of the cities which adopted the practice are different from the ones that made it known. Most of the cities that practice participatory budgeting in Brazil today are small or midsize cities, many among them have a very small associative tradition, most of them are concentrated in the South and Southeast regions of the country and tough most of the experiences of PB are linked to PT's administrations, there are plenty of experiences that are linked to other political parties. Table 5 below summarizes the most important characteristics of the PB experiences.

TABLE 5
Characteristics participatory experiences

	BY SIZE OF THE CITY	BY REGION	BY PARTY
NUMBER OF PB EXPERIENCES	UP TO 20.000 PEOPLE 31 CASES	SOUTH 39 CASES	PT 52 CASES
	BETWEEN 20 AND 100.000 PEOPLE 33 CASES	SOUTHEAST 45 CASES	PSDB 13 CASES
	BETWEEN 100 AND 500.000 PEOPLE 30 CASES	NORTHEAST 14 CASES	PMDB 9 CASES
	MORE THAN 1 MILLION PEOPLE 4 CASES	OTHER CASES	OTHER CASES
TOTAL	103	103	103

Source: Teixeira, 2003. Grazie, 2002.

It is easy to note which are the predominant characteristics of PB experiences: these are the ones concentrated in small or very small cities (64 experiences) of the regions South or Southeast of Brazil (74 experiences) most of them run by the PT (52 experiences). These cities have four characteristics which do not fully coincide

with those of the cities which introduced the PB as a practice: first of all, they have very little associative life. Associations are very weak and do not influence the PB. Second, the state administration tend to have more influence in the deliberative process, from calling the meeting to a direct influence in deliberative process. Icapuí in the Northeast region appears as one of these cases. It is a midsize and very poor city of the Northeast with a relatively successful experience of participatory budgeting in which 69,3% of the councilors of the PB are members of the local administration. Third, most of the small and mid-size cities in which participatory budgeting is being practiced simplify a little bit the process. This is the case in small rural cities in South region of Brazil such as Medianeira and Iguacu for which case studies are available. In these cities there is only one round of regional assemblies, most of the time there are not thematic assemblies and there is a simplification in the process of electing the PB Council (Teixeira, 2002). Fourth, there are also cases in which the cities in which the PB is implemented do not have access to enough resources to trigger a significative deliberative process. This is the case of the cities in the metropolitan region of Porto Alegre such as Alvorada and Viamão which have introduced the PB but have strong difficulties in transforming it into a distributive process due to lack of resources (Silva, 2002). Thus, we can see that although participatory budgeting is being extended to many cities in Brazil not all the experiences resemble the same deliberative and distributive characteristics of Porto Alegre.

We may differentiate at least two different kinds of experiences: the first kind is the one that emerged in Porto Alegre, was extended to Belo Horizonte still in the early nineties and is being practiced in cities such as São Paulo and Recife today.[7] These experiences share a lot of common aspects such as: all these cities had a relatively strong associative tradition with a very strong presence of community associations in the urban landscape. In all these cities, participatory budgeting involves a process of negotiation between the political administration which belongs to the PT (or to a left leaning party such as the PSB - Brazilian Socialist party) and community associations. In all these cases, participation is about 1% of the population (being a little bit less than that in São Paulo for scale reasons) and it roughly resembles the average income level of the population. Participatory budgeting in this first type of case shows the possibility of building an institutional form of participatory democracy based on the associative tradition created by community movements and their productive interaction with PT administrations. The results is the constitution of a more democratic political culture with strong distributive effects at the social level.

There is also a second case which involves small and mid-sizes cities in South and Southeast regions of Brazil. In most of these cases, the characteristics of the PB are a little bit different: all these cities have a weak or very weak associative tradition. In most of the cases, the PT governs these cities as a result of a demonstration process, as it has been the case in most small and mid-size cities in Rio Grande do

Sul. Participatory budgeting in these cases, is broadly simplified due to the easier conditions provided by the size of the cities. Most of these cities have a council which in general is constituted by the leadership linked to the administration or the PT itself, as is the case in Icapuí, Ceará. Yet, in most of these cases, participation is higher than in larger cities. It may reach levels between 10 and 20% of the population which may be explained by the city scale (Avritzer, 2002). Participatory budgeting in these cases, function well when two conditions are met: first, when the city is not very poor and may be able to establish a distributive process. Second, participatory budgeting is, in these cases, dependent upon the unity of the governing coalition (Silva, 2002), because, the associative movement in the city is weak and makes the process more dependent upon the characteristics of the administration itself. In these cases, we may see improvement at the efficiency level, but we seldom see democratization of the political culture.

Thus, it is possible to see that the practices that emerged at the societal level during Brazil's process of democratization can become an alternative source of democratic values at the public level in the case of cities such as Porto Alegre, Belo Horizonte and São Paulo. Once democratic values become available within the public culture, it is possible to bring them to the decision-making level through innovative institutional designs. Deliberative designs transfer innovation and the more egalitarian aspects of the public culture from the societal to the public level. Yet, the limit of the extension of these practices, is the characteristics of public culture itself. We have showed in this paper that in the cases in which innovation at the societal level led to new practices that are distributive and democratic impacts. We have also showed a second case in which the already existing innovation is extended through the political system to other setting in which the main characteristics of the societal culture remain the same. In this second case, success is determined by the administrative characteristics of the proposal and there is not a sharp change in societal culture. Though the two cases are different they show that the deliberative nature of the PB is able to create a new administrative standard which puts at stake Brazil's century old administrative practices and the social and deliberative inequalities associated with them.

NOTES

1 These attempts were materialized in a series of civil wars, the Cisplatine Campaign (1817-28), The Farrupilha Revolution (1835-45), the Platine Campaign (1849-52). See (Love,1971:13).

2 This has led to a big conflict in the early nineties in Porto Alegre. Uampa initially decided not to participate in the first editions of participatory budgeting. See Baierle,1998.

3 There are many usefull descriptions of the functioning of participatory budgeting and I will not make another one in this paper. For a full description of the process see, Bairle, 1998; Santos, 1998; Abers, 2000; Avritzer, 2002; Baiocc,2002.

4 To my knowledge there is only one city in the administration members vote in the PB Council which is Santo Andre.

5 Pavement has been the public good mostly demanded in Porto Alegre since the emergenc eof the PB. As of today 6 million square meters of pavement have been done. As a consequence of the levels of pavement that soil of the city became unpermeable and summer floodings increased. This has led to a technical veto on new chanelling of creeks.

6 The survey was applied in a sample of associated members who particpate in the the PB in Porto Alegre and Belo Horizonte. 5% of the members of existing assocations who participate in the PB were interviewed in each city . 122 interviews were carried in Porto Alegre and 80 interviews were carried in Belo Horizonte.

7 The size of the city involved is not the only characteristic of this group of cities. We could add to this group, cities such as Chapecó in Santa Catarina, Uberlândia and Ipatinga in Minas Gerais, Campinas in São Paulo and Caxias do Sul in the state of Rio Grande do Sul. For the characteristics of this intermediate case see Avritzer, 2003.

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Leonardo Avritzer

Professor of Political Science at Federal University of Minas Gerais - UFMG

Charles Sabel

COLLEAGUES:

What you have before you is the skeleton of a research agenda directed at what I hope are common concerns. It is in the form of an introduction to a paper, because we are at a conference, and papers are the conventional form of communication at conferences. I hope the form and the incompleteness of the paper will not distract you from the substance of the research agenda. To reduce the chances of misunderstanding, let me just state the core propositions at the outset:

Faced with a set of new challenges, the administrative state in the US, the EU and Latin America is evolving away from hierarchical and towards what we can loosely call decentralized, network forms of organization

If these new types of administration are to be democratically accountable, they will have to respond to a new kind of public sphere that differs in two ways from the traditional, Habermasian public sphere that emerged in association with the nation state.

Where the Habermasian public sphere aims to influence legislative decision-making, a public sphere that holds network administration accountable will have to be capable of monitoring and participating in decision-making, as much as influencing the general legislative frame within which that decision making occurs.

And where the Habermasian public sphere is directed to national issues and decisions, the new public sphere will have to link local monitoring and participation with higher, or more encompassing engagements, including the ability to revise decision-making frameworks.

There are fragmentary and fugitive signs of the emergence of such a new public sphere in the US and the EU.

But it is in Latin America that the new type of democratic public seems most likely to develop, because of the current co-evolution there of the public sphere and of public administration.

Thus countries such as Brazil are developing a potentially distinctive public sphere in response to the democratization of the oligarchic state, not the formation of the nation, even while state administration is increasingly "networked" as national economies, and the communities they shape, integrate into world markets.

But whether the post-oligarchic state will indeed be capable of effective, networked problem solving, and whether the emergent public sphere can indeed hold that state democratically accountable by monitoring and participating in decision making across a sufficiently broad range of policy arenas, while linking the relevant scales of action in each, are two very open questions.

So let's get to work, taking a close look at developments in Brazil from this perspective and using what we learn from this investigation to prod discussion of these themes in the US and the EU. One place to start might be the role, if any, of neighborhood educational association in school, reform, or of locally based watershed monitors in pollution control.

But these suggestions are meant only as illustrations of research projects that would test the general claim that new accountability mechanisms and new problem-solving institutions are co-evolving. The real questions, of course, are whether networked administration has the problem solving capacities many, myself included, attribute to it; whether the post-nation public sphere can indeed democratically domesticate the administrative networks, and whether that possibility, if more than a pipe dream, is being, or could plausibly be realized in Latin America or anywhere else at present.

The Introduction to the following "paper" note presents a fuller version of the same argument as it emerges from a comparison of current discussion in the US, the EU, and Latin America. It also contains pointers to recent work of my own that develops some of the key assertions. The next, and for now last, section of the "paper" presents a compressed overview of the operating mechanisms and foundational principles of the network or pragmatist organization as it is currently diffusing in both the private and public sectors. In include this because I think that "network administration," though loosely used, does in fact name a general and fundamental organizational innovation that can be precisely characterized. This characterization suggests, I argue, a reorientation in our understanding of governance, which may in turn direct where we look, and what we look for in a "new" public sphere. Although the material included raises the governance question and goes some way towards characterizing pragmatist or network governance, it breaks off

inconclusively, without raising, much less answering these final, crucial questions regarding the character of the new public sphere. Even if I could presently do more than wave my hands at these questions—which it far from certain—any serious attempt to answer them would give you the easy job of criticizing my insufficiencies rather than the hard one of advancing what do very much hope is a common project. I look forward to the discussion.

1. Introduction

The administrative state is challenged today in new ways. It must regulate exchanges with networked industries such as telecommunications and electric power, whose structure and possible evolution is often opaque to the primary actors themselves, and among networked firms, whose boundaries and obligations to each other are constantly in flux. It must protect the public against diffuse and rapidly shifts threats from, for example, the "non-point source" pollution that runs off countless farms, homes, and construction sites, and from new, rapidly mutating pathogens spread quickly through food supply chains by global commerce. As economic volatility—call it globalization—makes the risks of unemployment and other threats to citizen well-being effectively uninsurable, the administrative state must restructure such traditional public services as schools, continuing education programs, and job placement agencies, substance abuse and day care programs to "capictate" individuals and families—especially those who fare poorly with the "standard" offerings—to find their way not just in the economy, but in life.

There are sharp, revealing divides in the US, the EU and Latin America as to whether the administrative state can meet these challenges, and, if so, whether its eventual successes will increase or (further) diminish the democratic accountability of public administration. In the United States authoritative voices (Jerry Mashaw, Bruce Ackerman—for present purposes the Yale School) suggest that the New Deal state is unlikely to adjust to the new circumstances. Their empirical touchstones are the Environmental Protection Agency and the National Highway Traffic Administration of the Department of Transportation, entities created in the late 1960s and early 1970s, at the height of Congress's infatuation with top-down, command and control methods. From this vantage point the administrative state will fail, and fail unaccountably, at the new tasks for the same reason is largely failed, with little accountability, at the old: It depends on the expertise of officials who know vastly more than citizens, legislators, outside auditors and judges about what needs to be done, but still not nearly enough to solve the problems at hand. And it is subject to many, conflicting forms of legislative, judicial and managerial oversight that exacerbate, or at least make it impossible for agencies to correct the very problems the oversight authorities identify. Given these limits the best and perhaps

only way to secure social justice in a world that admits of neither effective social insurance nor the provision of capacitating services is to endow disadvantaged citizens with resources they can use to purchase privately goods and services that better their prospects.

Other, equally authoritative voices, such as Richard Stewart's, hold on the contrary that the New Deal state is not, and perhaps never was, as ossified as the Yale School and others maintain. Looking both to procedural innovations that might have been (in response, for example, to pressure from the judicial hard look) and at current developments at the EPA and elsewhere, Stewart sees the US administrative state as potentially able to serve new ends by adopting some combination of permit trading regimes to minimize the cost of social compliance with general regulations, and introducing non-hierarchic, networked types of decision making to allow general rules to benefit from, and in turn inform, local experience. My own work on the reorganization of public schools, long regarded as a paramount example of the unreformability of public bureaucracies, goes in the same direction. But Stewart, and other equally close students of recent developments of the US administrative state wonder whether the increased efficacy of networked administration may not come at the price of reduced public accountability, not least because the network arrangements blur the distinction between governed and government, allowing the latter to slip the control of the former.

These different assessments of the potential for administrative reform are reflected in the different reactions of the high federal judiciary on the one hand and the lower federal bench and State courts on the other. In areas such as school reform, fair (low-income) housing, and the reform of mental health institutions State courts have routinely assumed the feasibility of and insisted on organizational reform. On the authority of State constitutions or legislation they have required poorly performing institutions to meet general goals, such as the provision of an "adequate" education to poor, minority students as well as to rich, non-minority ones; to create systems for measuring progress towards those goals; to report the results of periodic measurement to the public, in ways that allow comparison of how much—or little—similarly situated institutions better the condition of at-risk groups; and to ensure that low performers learn from more successful ones. This form of judicial oversight, often undertaken in cooperation with legislative reform of the accountability system to which the affected institutions respond, seems to grow out of and encourage the diffusion of "network' administration. (on this see the paper with Bill Simon on destabilization rights just published in the Harvard Law Review and available in draft at http://www2.law.columbia.edu/sabel/papers/Chayes20clean.doc)

The high federal bench, on the contrary, is fixated on establishing the accountability, and limiting the discretion of administrative agencies, to the exclusion of any consideration of administrative efficacy. Textualist cannons of interpretation, limiting

agencies to classes of actions expressly authorized in legislation and insistence that judges defer t administrators are acting only with the intent of making law are only two of the nay doctrinal strategies deployed to this end. Such judicially prompted clarification of the sovereign pedigree of administrative decisions—express and legitimate delegation by Congress to an agency to make legally consequential rules, followed by the express declaration of a politically accountable administrative official that a decision is to have this effect—could well have the effect of centralizing decision making. But such is the indifference of both the high federal judiciary and the academics who comment on their decisions to question of administrative structure that is impossible to know whether this in an intended outcome, or simply the side effect of a general view that, despairing of any possibility of reform, simply seeks to minimize the harm that administration can to democracy.

In the European Union the view of the administrative renewal as feasible, even likely, but at the cost of democratic legitimacy, is more nearly a mainstream position than a countercurrent. Renewal seems feasible because in creating the Single Market while protecting the citizens of member states against many, changing threats to public health and safety, the EU has *already* established a web of novel, hard to characterize institutions—"comitological" technical advisory committees, networked observatory-agencies, the "open method of coordination" for comparing and revising national practices in many policy areas—whose overall, and generally acknowledged effect is to allow just the contextualization and periodic revision of general rules that might address the new challenges to the administrative state. EU experience broadly seen has been that the most satisfactory way to "harmonize" the regulatory systems of the member states is by instigating a process of mutual learning and monitoring in which the discovery of new possibilities changes the actors' preferences and leads to outcomes different from—and generally superior to—those that would have been produced by negotiation alone. Indeed the fact that the "winning" coalition in regulatory matters typically does not get what it initially thought it wanted is a good part of what makes the whole complex process politically sustainable. (form more on this, and reading of the EU developments as deliberative polyarchy—a type of network governance—see the paper with Josh Cohen at http://www2.law.columbia.edu/sabel/papers/Cohen-Sabel%20final.doc)

But this welcome increase in technical problem-solving capacity is widely regarded as a potential threat to democracy in the EU. It is unclear to what democratic public the problem solvers are to respond, and the currently compelling ways of constructing such a public seem at odds with basic features of the emergent system of network governance. Thus the EU famously lacks a demos: a natural community of language, sentiment, and historical experience coherent enough to embody itself, and its solidary commitments, in a parliament. On one reading the story ends there, because natural communities are the precondition of nation states,

which in turn are the precondition for political and social democracy. But a second, and historically better informed reading argues that the democratic nation state in fact arose from a circular relation between traditional contexts—substantive demoi—and a nascent public sphere: a space for the open discussion of the broad purposes of public power among equal persons ever more free of overriding group solidarities and everyday practical arrangements. Opinions formed in this public sphere direct political controversy, which shapes legislation, which orients the administrative apparatus, which operates to suffuse the original, traditional attachments with an aspect of civic or political loyalty and so broaden and deepen the public sphere. "Modern democracy and the nation-state have developed in tandem," Habermas, the leading exponent of this view, writes:

> Both have jointly produced the striking innovation of a civic solidarity that provides the cement of national societies. National consciousness emerged as much from the mass communication of formally educated readers as from the mobilization of enfranchised voters and drafted soldiers. It has been shaped as much by the intellectual construction of national histories as by the discourse of competing parties, struggling for political power.

To "conserve" (Habermas' word) the achievements of the democratic nation-state at the EU level it, is from this vantage point necessary to construct a European public sphere by refocusing media attention on "European" developments—so citizens in the various member states are discussing the same things at the same time—and by endowing the EU with political institutions similar to those of the nation-state—so citizens, from inveterate civic habit, will know (how) to address their public concerns to them. Brussels becomes the notional, if not the physical capitol of the EU, towards which the influence of the public sphere is directed, and from which the power of law, coursing through administration, flows.

But this historically attractive way of creating the democratic "principal" in the EU immediately encounters two closely related objections. The first is that the distinction between public deliberation and practical or technically informed action characteristic of this notion of the public sphere requires just the kind of cascading delegation of sovereign authority—from democratic people to legislature, from legislature to administration—which US experience demonstrates to be unworkable. Even if we can assume, the Yale school notwithstanding, that the future of US administration is yet to be written, there is little in its past that warrants the assumptions that elected officials, acting on behalf of citizens, can present clear rules and standards to agencies, and that those agencies will confine their activity to the efficient implementation of those rules and standards, subject to external monitoring. More generally, 'agency' problems are the notorious weak

link in the minimalist views of democracy that accept any duly elected legislative authority as a legitimate 'principal'.

More concretely—and here the second objection—EU regulation, and political deliberation broadly conceived, is *already* so distributed in administrative processes beyond the reach of conventional legislative oversight that the Habermasian conception of the public sphere cannot serve as a practical guide to reform. Presciently or inadvertently, as just noted, the EU has created a system of harmonizing administration that works as much "horizontally" as "vertically," and more by federated influence of lower-level units on higher ones than by top-down determination of ends and means. If the EU public sphere turns out to be the public sphere of the nation state writ large, it is unclear to whom it is to address itself. Intuiting this dilemma, but unable to resolve it, the practical architects of political reform, convened in the Convention for the Future of EU have been careful not to write the new problem-solving institutions out of the draft constitution, without finding a way of establishing their democratic legitimacy by writing them in. Conversely, those familiar enough with the accomplishments of the new problem-solving institutions to count as their advocates are agnostic, verging on pessimistic, with regard to their democratic aptitude. As in the US I believe that close attention reveals a more subtle and promising interplay between administrative adjustment and effective public oversight. But for now the stark contrast between efficacy and legitimacy dominates public debate.

In key Latin American countries such as Brazil, Mexico and Argentina the prospects for accountable administrative reform are different again. If the administrative state is widely seen in the US as maladapted to current tasks but perhaps accountable to a vigilant judiciary, and in the EU as adaptable but unaccountable to any plausible public, in these countries the administrative state and the public sphere are evolving together in ways that suggest the possibility— but hardly the inevitability—of an adaptive administration responding to a novel pubic. Consider the case of Brazil as rendered by Avritzer and other participants in this meeting. On the one side the clientelistic, patrimonial state bequeathed from colonial times, and engorged with populism and management of import substitution, must open itself to democratic supervision while reforming to meet challenges different in degree, not kind, from those faced in the advanced countries. Hence a profusion of new, more or less "autonomous" entities at various levels of government, at times explicitly modeled on US examples, but often "networked" on lines that the EU debate tends to acknowledge even if the US debate does not. On the other side is a potentially new public sphere, or, more exactly, constellation of new publics, born not in the struggles of nation building but rather in the long fight to democratize oligarchic national states. The collection of publics or emergent public sphere, born of social movements that mistrusted the day-to-day clientelism at the street level of the old state

and reviled the anti-democratic isolation of its peak institutions, has two characteristics that mark it off from the Habermasian model. First, it is concerned at least as much to monitor specific state actions as to influence general policy; and when decision-making is decentralized, as it often appears to be, the monitoring shades into a form of co-decision making, or at least a kind of continuing, informed contestation of technical expertise by citizen users of public services. Second, the new publics tend to be local, or at least sub national, without being isolated in a particular setting. Municipal participatory budgeting as Avritzer presents it illustrates both features: citizen assemblies, with members drawn from different neighborhood-based associations, review the performance of municipal road construction agencies and water utilities, helping to determine the sequence in which districts are connected to the existing networks, and in some cases the balance of investments among road building, expanded water service, and other classes of municipal activity.

Could the new post-national public sphere that the democratic domestication of network governance seems to require arise from such a matrix? To anwer that question we need to get a better idea of just what network organization is, and how it might effect regulation and the public sector generally. The next section goes same way towards addressing these issues. Then we need to step back from this account of the emergent form of problem solving to reflect on its possible implications for democratic accountability and democracy generally. Finally would could begin to assess Brazilian and Latin American developments more broadly in the light of the our revised conception of what governance, and democracy, need to do. The "paper," as noted, does not address these issues. But I very much hope the conference will. It is with that goal in mind that I invite you to read on.

2. Thee Types of Pragmatist Organization

In the century before 1980 the canonical organization was hierarchical and closed. Headquarters set goals, parsed complex tasks into simpler, more manageable ones; organizational routines specified how to parse, execute and review the compliance of tasks. Subordinates were rewarded for complying with instructions; middle managers checked the conformity of activity to plan. After 1980 the canonical organization is federated—decisions of higher units are shaped by lower ones and open—the lower units can be formally outside the organization. Or, to capture the idea that information in the new organization flows up and down as well as sideways, they are said to be networked. General designs are set provisionally by the highest level and revised in light of proposals by lower level units responsible for executing key modules or subsystems. The organizational routines define methods for choosing provisional, initial designs and revising them in the light of more detailed, partial proposals. Collaborators are rewarded for achieving broad goals according to

standards defined as part of the process by which the goals themselves are set. To get a more precise idea of how these new organizations work, and of the principles informing their design, consider three variants of the networked organization as it appears in both the private and public sectors.

Take first the *deliberately innovative organization*. This is the canonical case of the new, networked organization: the firm—it almost always is a firm—whose very purpose is to produce innovative products or services. Perhaps the best documented example is of design and production in the automobile industry. The process starts when, say, the new-van design team in an automobile firm sets the general performance characteristics of the vehicle by benchmarking the best features of current vans and exploring which innovations under development can be incorporated in its design. To benchmark the potential of developmental work the team may ask for engineering simulations of possible outcomes, "flash market" a product embodying a potentially valuable feature, or otherwise try to test the actual reaction of buyers to some approximation of the design they are exploring. Assessing the results of these probes, and again guided by reference to leading examples and comparison of possibilities, the team next provisionally subdivides or, to take a term from cognitive science, "chunks"[1] its general goals into subtasks—the design of an engine, or heating, ventilation and air conditioning system—and chooses a specialist team from inside or outside the parent company to realize the initial specifications. (It may seem unduly fussy to refer in this connection to "chunking" rather than the more familiar "modularizing," especially since the latter is often used loosely in the automobile industry and elsewhere to mean the former. But modularization, more strictly speaking, aims at the creation of fixed, black boxes whose performance is durably defined in an interface listing the output returned for any input. Where the corrigible provisionality of design choices being describe here is useful, modularization *strictu sensu* is, as we will see below, risky, even impossible.) After this initial chunking separate project teams elaborate all the provisional subsystems concurrently, applying to that task the same kind of evaluation of competitors'successful efforts and developmental possibilities used in the van team's first round of benchmarking. In addition, they benchmark the production processes central to their eventual products to ensure that the methods employed will meet or surpass the efficiency of their most capable competitors. Engine plants, for instance, will have to produce engines that are at least as cheap and warrantable as those of competitors making similar engines in comparable volumes. Then the initial overall goals are modified by the methods of simultaneous or concurrent engineering, e.g. the engine-design group may find a way to better its target specifications or to cut its manufacturing costs if it can persuade other component groups that design characteristics should be modified accordingly. Refinement of this iterated co-design continues once production begins by means of just-in-time and the error-detection and

correction methods associated with it. In just-in-time production, parts are supplied to each work station only as needed: ideally, one at a time. Hence disruptions are immediately visible. A breakdown at one station halts production by stopping the flow of parts to downstream operations. To assure the flow of production, therefore, the source of disruption must be identified. This typically requires tracing long causal chains back to improbable origins by insistent questions sometimes called the "five why's". For example:

Why is machine A broken?	No preventive maintenance was performed.
Why was the maintenance crew derelict?	It is always repairing machine B.
Why is machine B always broken?	The part it machines always jams.
Why does the jam recur?	The part warps from heat stress.
Why does the part overheat?	A design flaw.

Thus error-detection and correction, like benchmarking and simultaneous engineering, reveal possibilities for improvement in unexpected (mis-) connections among the parts of complex endeavors; and the cumulative effect of these results is captured in improvements in the benchmark standards for various production processes.

Benchmarking, simultaneous engineering and error-detection methods like the "five why's" are counter-intuitive from the vantage point of classical organization theory. In classical theory, routines are questioned only in exceptional circumstances. It is simply oxymoronic from this perspective to try to do what the new institutions do as a matter of course: routinely question the suitability of current routines for defining and solving problems. We can think of these new institutions as pragmatist: They systematically provoke doubt, in the characteristically pragmatist sense of an urgent suspicion that routines—habits gone hard, into dogma[2]—are poor guides to current problems.[3]

As a second instance of such pragmatist institutions consider the *High Reliability Organizations (HROs)*. HROs are well, but incompletely designed to perform without fail such extraordinarily demanding tasks as generating electric power through nuclear fission, launching and recovering jet aircraft rapidly from and back onto pitching, greasy flight decks, launching and recovering space shuttles, or fighting forest fires as they race through rough terrain. The designs are necessarily incomplete because the conditions under which the specified tasks are to be accomplished are changing continuously in more or less subtle ways. If the organization is not adjusted accordingly, it fails, catastrophically. In the pragmatist terms just introduced, HROs become disastrously unreliable if they assume that routine, (nearly) invariant success is the result of following invariant routines; and the organizational challenge is to avoid accidents day after day without imperceptibly making this assumption.[4]

Key to this are error-detection and root-cause analysis disciplines of the sort broadly familiar from the production/operations level of the innovative organization. In the setting of HROs, the most important and characteristic of these is Near-miss reporting and analysis. Near misses of course are accidents that only accidentally didn't happen. So the near misses—and beyond that "out-of-control" sequences that nearly produced near misses—are the urgent analog in the HRO to the line stoppages in a just-in-time system. Both trigger root-cause analysis meant to uncover not only the proximate cause of the incident, but to eliminate, through redesign of the organization if necessary, the background conditions which generated the immediate source of danger.

Note here a circumstance to which return later when considering governance—the root-cause analysis regimes are often regarded as a key element in the governance of HROs, and when that is the case they are subject to regulatory scrutiny. For example nuclear power plants in the US are rated in part on how effectively they respond to reports to reports of anomalies at other plants that might be of relevance given their own set-up, and so on.

New Public Services are third case of pragmatist organizations. This type of institution is little discussed in the organizational sociology literature, but is receiving increasing attention in various domains of policy studies. Well documented examples are schools in Texas, Kentucky, North Carolina and elsewhere in the US that actually teach poor children of color to read and do mathematics with proficiency comparable to that attained by rich, white pupils. The new organizations are like HROs in being designed to achieve a single, complex task—teach children to read and use mathematics—and in relying on error-detection to compensate for design deficiencies. But there is an important difference. Where the design gaps are in HROs are, roughly speaking, small in relation to the overall structure (that is why we say it is well designed) the new public service the situation is reversed: there is lots of "gap" and little by way of consolidated design. No one, in other words knows how to build a school system that produces the desired result. Instead the institutional solution is to build an organization that uses error-detection and correction at the lowest levels to find ant what works, and then adjust the higher level structures to generalize that behavior and encourage more refined error detection, and so on. With regard to reading, for example, all students learn by some idiosyncratic combination of decoding strings of letters/phonemes (phonics) and derivation of the meaning of words and sentences from context (whole language method). Teachers identify the strengths and weakness of each student's mixture of strategies by sampling their skills in brief, daily sessions, and suggest improvements. (This might be called first-order error detection and correction.) The performance of students in the same grade is measured periodically state wide by a standard test, allowing for the comparison of the performance of teachers within schools, schools, and districts. (second-order error

detection.) The job of principals in this system is to create conditions in the school for generalizing the successes of the most successful teachers, and The job of the job of the principals' superior—the district supervisor—is to create conditions for diffusing the successes of the most successful principals.

In this way the reformed school is invented through the piecemeal, but eventually comprehensive improvement of a crude, but serviceably provisional starting structure that supposes only the broadest, non-vapid agreement on goals—educational achievement (by mainstream measures) should not vary across groups in culturally salient hierarchies, and gaps should be closed by leveling up, not down—and methods—teachers must aid students to improve their individual bundles of learning strategies, and administrators must aid teachers and other administrators in doing this.

Accepting now as a stylized fact that the new organizations operate successfully by application of these methods, and leaving for another time questions concerning the morphology of and methods for constructing the networks presumed in what follows, we return to the classic questions of bounded rationality, efficiency and governance and try to provide a consistent and conceptually plausible account of this success.

3. Bounded Rationality, Efficiency and Governance in the Pragmatist Organization

Rethinking Bounded Rationality

The centrality of search routines to the new organizations suggests that there is an alternative to the decomposition of tasks as a solution to the problem of bounded rationality: Under volatile conditions, when it is given that no one can know the whole answer to the design question we face, the way to respond to bounded rationality is to find actors who are already solving (part of) the problem we will turn out to be trying to solve. To be workable any such problem-solving search (regardless of where in the overall design or production sequence it is conducted) will, at a minimum, have to Disentrench enquiry, directing attention to unfamiliar solutions, while it Produces sufficient information about advantages and disadvantages of rival possibilities—the solution space—to become Self limiting. If it doesn't meet these requirements the search will be uselessly redundant—when you don't know what you are looking for it is especially unproductive to look where you always look—or outright destructive, sending the actors off on an endless fool's errand.

Benchmarking and error detection do indeed oblige the actors to search for solutions in a novel, initially open, but ultimately bounded space of possibilities: the set of best current or potential designs (benchmarking) or the activity chains that

might have caused a particular breakdown (error detection). The initial canvas of design solutions is of necessity novel and open because it must consider responses that are "like," but potentially better than current practice on at least some of many dimensions, and "like" has no determinate meaning in advance of a particular search. Indeed, to search for likes is to invite surprises. The point of the search is precisely to uncover an unsuspected but highly informative resemblance.

Consider by way of example this telling episode in the evolution of the modern paintbrush. A company is trying with little success to produce the traditional house painter's brush with artificial bristles. Even an accomplished artisan can't apply a smooth coat of paint with the synthetic bristles. The question arises: what is a paintbrush like? If a trowel, then the performance is determined by the shape of the bristles' tip, and the company's problem is to find an artificial equivalent for the split ends of natural hairs. If, however, paintbrushes are like pumps, performance is determined by the contour of the channels formed by the bristles, and the next step is to reposition the artificial bristles to channel paint correctly.[5] In this case the brush was more like a pump than a trowel—but this result, of course, is provisional. In more artfully inclined hands a brush may need to be less a pump than a trowel, sling-shot or eyedropper.

As in this example, each possibility considered in metaphoric benchmarking provides a vantage point from which to evaluate the strengths and weakness of the others. Hence the search produces something "like" a provisional taxonomy or map of accessible solution strategies in relation to each other. In this way it is self-limiting: Once you have a serviceable map of the solution space, you stop doing cartography and decide where you want to go.

Robustness as Highly Dynamic Efficiency

Before we can ask about the efficiency of organizations in high-volatility environments, however, we have to clarify the question. Efficiency is a static concept, or rather a concept for stable environments. The efficient solution is just the least-cost means of reaching a known end. When the ends are various, and by some measure closely related, it can still be meaningful to speak of "an' efficient solution or a set of these. But when the ends become more various and less well specified it no longer makes sense to speak of optimum or efficient solutions. Instead we can ask whether our problem-solving technique is robust, meaning that it can be expected to produce workable answers turbulent task environments. Think of robustness as highly dynamic efficiency.

To underscore this point let me note here the misleading incompleteness of Simon's well-known story about two watch-makers, Tempus and Hora, whose competition is intended to show the robustness (resilience in the face of disruption) of hierarchical modularization. Tempus and Hora, you will recall, made similarly

complex watches of about 1,000 parts each. But Tempus, the craftsman, assembles each watch from 1,000 pieces, while Hora, the mass producer, makes sub-assembles of 10 pieces each and then combines these into the final product. Simon shows easily that unless the probability of disruption per unit time is extremely low, Tempus almost never completes a watch, and the typical disruption destroys an extremely valuable, nearly finished piece. Hora completes much more work and losses much less in each disruption, so modularization seems robust.[6] And it is in comparison with craft production of large numbers of extremely complex machines.

But modularization is plainly not robust in our current world, where key module makers—meaning here sole-source suppliers of indispensable components—are routinely destroyed by natural catastrophes or the complete devaluation of a core capacity through a competitor's innovation. The robust strategy in this world is one where there is no difference between setting up the production system and repairing or replacing it in case of disruption; or, put another way, where the same principles that generate the initial set-up also generate innovative transformations of that first design as circumstance require. These are the principles that our robust producer, Quaesitor, follows when she searches for collaborators who are good at searching for collaborators all the way down. In this system, if any of the producers "breaks," the broken one and its collaborators find at least one replacement or substitute.

The destruction, by fire, and the almost instantaneous, collaborative reconstruction of the capacity of a key Toyota supplier illustrates the robustness of Quaesitor-type re-chunkers. When it burned down in 1997, Aisin's Kariya plant 1 in Kobe was the extraordinarily efficient, sole-source supplier to Toyota of P-values, a relatively simple, but high-precision component of an anti-skid break-control mounted on all of the assemblers' makes and models. True to its just-in-time discipline, Toyota had only two-days' worth of P-values in inventory on the day the fire broke out; when that stock was exhausted, the assembly lines stopped. But by 3 days after the fire a congeries of a few Aisin suppliers and many other firms in the Toyota group—very few with prior experience in manufacturing this particular part, all presumably motivated by solidarity and the self interested desire to return to normalcy and distinguish themselves on the way—were producing more than a hundred types of P-valves in their own facilities. By 5 days after the fire two of Toyota's Kobe plants were reopened; 3 days later car production was at more than 90 percent of the pre-fire level; a week later there was no shortage of P-values at all. Ultimately 62 firms became emergency producers of P-values; these producers themselves relied on more than 150 emergency suppliers. So devastating had been the fire that none of the participants had access to the precision tooling that Kariya plant 1 used to make the original part. Aisin did contribute to the recovery by installing thousands of additional phone lines to respond to requests for information. But neither it nor Toyoda attempted to direct the reconstruction effort.

The key to the extraordinary success was the participants' vast, common experience of the Toyoda variant of iterated co-design: Aisin could characterize the part and the production process in general terms—chunk them; the emergency producers could devise, starting from their own experience, many different ways (some quite innovative) of achieving these ends. Then they could chunk the processes they were contemplating so that their suppliers could do the same with respect to subtasks. So, as Quaesitor would have expected, the same disciplines that generated a network of "module makers" continuously searching for ways to improve also generated the capacity to search out alternative solutions if one of the network's module-making nodes fails. In a malign world this distinction between efficiency and robustness would translate into an impossible choice: we would have to either increase efficiency or increase robustness, without knowing from one day to the next which is called for. In a more benign world we would expect that increased robustness would increase efficiency as well, so that measures that help us enhance performance in a volatile environment also improve operations under more stable conditions. This is in fact what we observe with the new organization. I suspect that the overlap between robustness-enhancing and efficiency-enhancing mechanisms explains a good deal of the explosive diffusion of this new institutional type.. The consider as an illustration of this overlap benchmarking and the metaphoric learning associated with it. In a volatile environment we expect tomorrow's conditions to differ sharply from today's. So minimal prudence demands that we continuously benchmark new developments to avoid disastrous surprises. But we just saw that benchmarking searches inform us about *all* the possibilities in the—expanded—solution space. That means that so long as the environment has not cooled down to the organizational equivalent of absolute zero, where benchmarking itself is unnecessary because conditions never change, these comparisons tell us new things about solutions we already know even as they reveal solution-strategies we had not foreseen at all. This is surely an important part of the reason that comparison of additional variants often improves the reliability the eventual designs rather than degrading it.

Something similar is probably at work with the second mechanism: concurrency. Concurrent development—in which "upstream" and "downstream" steps proceed simultaneously, each taking account of the (changes in the) requirements of the other—is almost unavoidable when rapid change puts a prohibitive penalty on missing, or being late for a market, But like benchmarking, concurrent development sheds new light on familiar designs and practices even while illuminating new environments. In particular concurrency calls into question taken-for-granted assumptions about the relation among components in any subsystem by prompting chains of what-if questions about how perturbations in the environment would reverberate through the inner structure of the complex. So in all but the most stable settings,

some concurrency probably leads to efficiency-improving discoveries about shortcomings in familiar arrangements while also increasing robustness.

Governance

Governance in the classic organization, we saw, is on the principal-agent model, or its stake-holder variant. The agent is punished for using her discretion to make self-interested use of gaps or imprecision in the principal's plan. She is rewarded for faithfully following that plan, or, better yet, using her discretion to fill gaps and correct mistakes in a way that realizes its master goal. Principal-agent governance is plainly unworkable in the pragmatist, search organization, because in such organizations final goals are the product, not the starting point of organizational activity. In this network setting the very distinction between principals who set plans and agents who execute them is blurred. "Agents"— meaning simply those whose relatively narrow responsibilities put them "lower down" in the organization—certainly can't be held to account for realizing the "principal's" original plan or complying with rules specifying their tasks because there was no plan, and hence nothing from which to derive detailed task assignments.

How, for starters, can accountability can be established if not by looking backwards? One alternative is to by looking in effect sideways and forwards, or rather sideways at how well others are looking forwards. An actor in a pragmatist organizations is acting accountability when she learns at least as much as other collaborations about the unfolding possibilities for advancing (and re-defining) the joint project, and discloses what she learns. Accountability thus becomes a matter of peer review: All the actors, or some relevant subset of them, assess the capability and intention of each to engage in iterated co-design or its production-level equivalents. Accountable behavior no longer entails compliance in the sense of rule following, but rather provision of a compelling explanation for choosing, in the light of fresh knowledge, one way of achieving the common goal over others. Hence the accountability systems of pragmatist institutions will be characterized by declaration of broad goals or performance standards that are explicitly treated as provisional and subject to revision through the actors' peer reviews of their own disciplined learning.

Such a rolling review of purpose and performance will only be possible if at least some of the information needed for the substance of collaborative problem solving in particular cases can be used for benchmarking the abilities and probity of current and potential partners. By making each party's facility with shared and highly revealing problem-solving techniques transparent to the others, pragmatist organizations make current collaboration (or the exploration of possible joint work) richly informative about the potential and risks of partnership. A firm that easily ferrets out the source of errors with five-why methods will presumably do better at solving new problems, and hence be more reliable collaborator, than one that gets lost

in the maze of its own confusions. Similarly, the mutual transparency that results from co-design disciplines makes it possible to detect, and attempt to correct, potential problems before they become disasters. Call the fusion of substantive and evaluative knowledge that allows an organization to learn as it monitors accountability (and vice versa) learning by monitoring. The explosive diffusion of pragmatist disciplines and the success of the new organization generally strongly suggest that such learning by monitoring is in fact workable at the level of individual projects or the operation of relatively small units, where "workable" here means only that show-stopping opportunism and inaptitude are detected, not that all interests are perfectly aligned, eliminating every trace of power. At the limit, If participation in the new disciplines did *not* facilitate detection of dangerously incapable or opportunistic partners, the spread of pragmatist organizations would have been quickly stopped by some variant of the hold up—the collaboration-destroying use of collaborative discoveries—that classical organization theory long took to be a fatal threat to just the sort of vertically disintegrated co-design commonplace today.

But the very connection between problem-solving substance and partner evaluation that makes learning by monitoring an instrument of governance on the project or small-unit level seems to rule it out as a mechanism for governing large and complex institutions such as multinational firms, public service providers or regulatory systems that encompass many different kinds of projects. Deciding to allocate scarce resources among these different, perhaps competitive projects, or to add entirely new ones, is of course a central task of such organizations. The ability of a project group or unit to demonstrate that it and its collaborators are highly capable of developing new tasks from current ones plainly bears on, but cannot alone decide, such questions. How, if at all, can such encompassing organizations select projects and maintain accountability by looking forwards and sideways. Put another way, is there some higher-level, project-spanning device, compatible with and perhaps analogous to learning by monitoring, for disciplining choices about the direction of collaboration and the identity of collaborators with the help of current, cooperative experience?

We can begin to outline the features of such a governance mechanism by listing the constraints it will have to respect in operation, just as we did in describing what turns out to be the closely related mechanism of dis-entrenching search. First, the forward-looking accountability mechanism must of course produce categories for comparing, and eventually ranking, different projects. Otherwise it is useless as a device for project selection. But second, in establishing this comparability, the accountability mechanism must encourage the exploration of new strategic goals, not restrict it by only rewarding search for better means to one or a limited range of given and unchallengeable outcomes. Recall that the aim of the metaphoric benchmarking key to the pragmatist institution is precisely to encourage the search for new solutions or projects outside the realm marked out by routine. A governance

mechanism that created disincentives to just the kind of searches the organization was designed to perform would plainly be self defeating. Thus the first two conditions just rephrase, and apply to the level of strategic choice, the conditions on disentrenching search: accountability and search mechanisms in pragmatist organizations must encourage investigation of novel goals, while using mutually illuminating comparisons among the results to limit the search and establish criteria for choosing a course of action from its results.

A third and closely related condition is that the pragmatist governance system domesticate, not generate or exasperate power struggles in the organizations to which they are applied. This seems like it should go without saying: a governance structure that invites opportunism is an institutional equivalent of a doctor who systematically violates the Hippocratic oath. But notice that governance in pragmatist organizations is likely to be especially susceptible to such counter-intuitive abuse because of the characteristic circumstances that give rise to opportunism in them. In hierarchies the occasion for opportunism is the agents' informal—unobserved and discretionary—revision of formal rules.

Since the unrevised rules are simply unworkable (working to rule is a famously effective way to paralyze a plant), the informal adjustments that make the organization function create opportunities for opportunism as well. The governance system with all its incentives and reviews is in some sense (and however flawed) a corrective or supplement to the self-limiting distribution of decision-making authority hard-wired into the hierarchy itself.

In the pragmatist organization as stylized here, in contrast, the actors routinely exercise discretion, generating or modifying the organization structure even as they do. We can say either that the emergent or informal network of decision making is the (new-model) formal structure. Or—in view of the way flexible formalization makes explicit much tacit knowledge and discretionary action without reducing it to a traditional rule set—we can say there is neither a formal nor an informal structure in the traditional sense. In this setting governance, in imposing procedures for high-level, strategic choices, creates new occasions for opportunism rather than merely providing a (perhaps faulty) means of limiting existing ones. Consider, for instance, the case where the governance rules ignore the second constraint and institutionalize preferences for particular means or ends. In that case the units and project groups are tempted to manipulate the center into selecting the rules that show their own efforts in the best possible light. Indeed the ensuring struggles for power, and the attendant disincentives to guess wrong about what will be rewarded, is surely one of the mechanisms by which a misgoverned pragmatist organization chokes off the very searches it is intended to pursue.

The fourth and final constraint is simply transparency: the governance mechanism must enable stakeholders—regulators, the public, employees, investors, suppliers,

creditors—to look into the organization, and into the system of governance itself. The background assumption here is simply that governance arrangements, like all other aspects of the pragmatist organization, are provisional, and designed to be improved in view of the experience they help generate. A governance system whose key purpose is to facilitate strategic choice among competing projects should allow stakeholders to go some way towards corroborating the eventual choices by looking in the relevant detail at the projects under consideration. Or, if the governance system fails to provide such corroboration, it should at least reveal enough about its own operation to allow improvement the next time around.

In posing the problem for pragmatist governance the preceding list of conditions has also telegraphed a general solution: A pragmatist organization can govern itself subject to these constraints by applying the core principle of iterated codesign to the choice of strategy or goals itself. As a first step in a highly stylized version of such a process the center—acting, perhaps on behalf and with the help of representatives of the individual subunits—metaphorically or openly benchmarks its overall objectives, looking for goals "like" the current ones, but arguable better on some dimension. Each of the federated units then does the same with respect to the broad task for which it is responsible; and the general institutional goals are, if necessary, revised in the light of the interim results. At least in theory, in metaphorically benchmarking their goals the overall organization and its subunits make the formulation of their purposes, and what kinds of projects should accordingly be rewarded, as open as, and therefore fully responsive to, pragmatist searches at the project level. Through iterated pooling of the benchmark goals the organization and its units set the general priorities with which to rank projects. So long as the goal-setting process remains open in this way there is little incentive to try and seize control of it: If currently successful projects will routinely be compared with a (limited, but ex ante unspecified) list of potential alternatives, no group can institutionalize selection criteria that are reliably favorable to itself. Hence there is no incentive to struggle for control of the goal benchmarking process (except, of course, to replace it with some method that does allow the powerful to fix purposes their way). Brief accounts of a range of pragmatist governance mechanisms from the private and public sectors indicate how these general principles can be brought to bear in particular contexts. Take first the case of the Illinois Tool Works, a mid-size conglomerate with $9 billion dollars in annual sales and nearly 50,000 employees world wide. One of its divisions makes plastic and metal components, fasteners and assemblies, industrial fluids and adhesives, fastening tools, and welding products for the construction, automotive and consumer durables markets. Another makes consumer and industrial packaging, as well as product identification and quality assurance equipment for the food retail and service, food and beverage, and capital goods industries. The firm is organized as a federation of some 600 units. These are financed by headquarters,

to which they for the use of corporate research and development facilities. But within these limits the units are largely independent. Each is responsible for setting its own goals, and is held accountable for outcomes. Because of this focus on components and small subsystems, and the flexibility of its individual units, ITW has flourished where mega-module makers, in their rigidity, have floundered. The key governance rule for goal setting in ITW is derived from Pareto's rule of thumb that only a small fraction—about 20 percent—of all the causes of an outcome account for some 80 percent of the total effect. The 80/20 governance rule obligates the units to regularly re-determine *which* 20 percent of their activities account for (roughly) 80 percent of their profits; to built up these disproportionately beneficial activities; and to spin off or simply abandon the rest. But each unit's sales to its customers bundle many different kinds of goods and activities: particular co-design services; unusually short product-development cycles: innovative use of a particular materials or the processes by which they are worked. So, following the rule, the unit's fist task is in effect to do a root-cause analysis of the grounds of its own current successes, and redirect its strategy according to the results. That done, the unit must metaphorically benchmark the new strategy by exploring potential uses of its newly re-characterized capabilities that are "like" the currently successful ones. Because judgments about the viability of strategies discovered in this way always contain a speculative element, a subsidiary governance rule provides that managers are not penalized for being wrong (once or twice), but face immediate sanctions if they are caught pursuing strategies that have not been disclosed and justified to headquarters. This second rule gives managers an incentive to (temporarily) immunize themselves against the risks of incorrect decisions by increasing the transparency of their decision making to headquarters, and so to other units in the firm and outside stakeholders.[7]

A second illustration is the governance system of Cisco Systems, the leading maker of network routers, switches and interface devices. To remain competitive in one of the worlds' technologically and commercially most volatile markets, Cisco invests of course heavily in research (roughly 17 percent of sales in recent years). But the distinctive aspect of its strategy is a policy of acquiring technologies or products pioneered by other, usually much small firms, and then working with the managers of acquired firms to develop them. As of mid 2001, XXX years after its founding, Cisco had incorporated some 75 units through A & D. This policy depends in turn on two governance rules. The first, dis-entrenching rule obligates business units to conduct a "make or buy" review when preparing their annual business plan. This requires each unit to compare the strengths and weaknesses of its current produce or service, and closely related variants of these, to those alternatives under development or already produced by competitors. Because Cicso's headquarters has rich knowledge of the changing needs of end users through its sales force, and many ties to the research community, business unit managers have every reason to identify and

evaluate potential acquisition targets before they come to general attention. In case of an acquisition, a second governance rule provides that the inside managers are rewarded for retaining the managers of the target firm, and integrating them into Cisco. Together the two rules not only encourage (as at ITW) regular reassessment and occasional brusque change of strategy and the business—unit level, but also, by making outsiders into insiders, increase the cognitive diversity of management generally, and so facilitate the next rounds of assessment and change.[8] And of course business-unit changes can in combination lead to large changes in overall strategy.

The public-sector equivalents of these dis-entrenching governance rules take the general form of an obligation that each unit measure itself against some general goal or performance standard—reliable and safe operations, continuous improvement in service provision—and correct shortfalls revealed by comparison with the performance of others facing similar situations. A straightforward regulatory application is the requirement to undertake near-miss analysis in the US nuclear power-generating industry. Utilities in the industry must report disruptions in their operations to the Institute for Nuclear Power Operation (INPO), an industry-funded entity ultimately responsible to the Nuclear Regulatory Commission. INPO officials sift these reports to distinguish harmless disruptions from dangerous ones. Thorough analyses of the causes of the dangerous disruptions, and ways of preventing them, are then circulated as Significant Operating Experience Reports, or SOERs. Industry Operating Experience Reviews then periodically assess the ability of particular plants to effectively use the SOERs and other means to improve their own affairs. For purposes of this review, a team of specialists in a variety of areas evaluates the plant's troubles since the last INPO inspection, paying particular attention to the plant's own reports on how it has responded to SOERs.

Where minute variations in daily operations are less likely to signal the possibility of substantial, hidden risks, the government can require the regulated entity to scan periodically for possible hazards and present a plan for mitigating those that it identifies. A regulatory oversight body then evaluates the adequacy of the plans, and the steps to realize them, against the benchmarks set by the best performers.

The shift in the US in the 1990s from poke-and-sniff (organo-leptic) methods of ensuring food safety to the hazard analysis of critical control points (HACCPs) shows the drift of developments.[9] In the organo-leptic method an inspector from the Federal Safety and Inspection Service examines every head of cattle or chicken being dis-assembled in a slaughterhouse for quality defects and especially signs of pathogens. The limitation of the method of course is that some pathogens may not be detectable by the usual examinations, so that meat products leaving the processing plant are not assuredly safe; and even if they are, pathogens introduced at later stages of the food supply chain would notice. Under the HACCP regulations introduced by the US Department of Agriculture, meat and poultry processors have to

identify all the points in their production processes where pathogens are likely to introduced; detail how they will reduce these risks and verify, by testing, the success of the adequacy of their measures. The HACCP plan must be complemented by a Standard Sanitation Operations Plan detailing the plant's regular housekeeping measures. The role of federal inspectors shifts from direct examination of animal carcasses to verification of the processors' hazard reduction systems. This verification starts with assessment of the adequacy of the HACCP plan (and the companion Standard Sanitation Operations Plan) and includes review of the plants test results as well as independent testing by the inspectors. Eventually the HACCP system is to cover every link in the food supply chain from farm to plate.[10]

The US Securities and Exchange Commission is shifting the regime governing financial disclosures by publicly traded companies in an analogous direction. Having re-discovered in the recent stock-market bubble that complex rule systems are easily gamed by managers with powerful financial incentives to do so, the SEC is requiring firms to practice "critical accounting": In reporting their financial results, firms will have to identify the critical accounting issues where their choice among arguably legitimate but rival methods of valuing results made a material difference to their statement of overall performance. For each of these issues the firm will have to document the alternatives considered; the valuation that would have resulted from the application of each; the reasons for the choice of the method actually used, and the key participants in the decision-making process that produced the final result; and even an assessment of the risks to the regulatory system as a whole that would eventuate if the firm's preferred method were broadly adopted.

With regard, finally, to complex public services, the dis-entrenching governance rules typically requires operating units to formulate and periodically revise strategies for increasing rates of improvement towards a general end. In the case of pragmatist public school reform discussed above, for example, the general goal is to reduce and eventually eliminate the difference in performance in key subjects such as reading and mathematics between affluent, white students and poor students, who are also often of color. In Texas the State governance regime accordingly requires period testing in these subjects by means of sophisticated standard test that (now) rewards the ability to conceptualize rather than rote learning. Each school must report the results of these tests disaggregated by economic and ethnic groups, and the State pools the data so that parents with children in a particular school can compare the rate of improvement of improvement of the relevant subgroup in that school to the 39 other schools in Texas demographically most similar to their children's. Further dis-aggregation at the district or school level then yields information about the performance of particular teachers and administrators that can guide further reorganization.

In elaborating these general features of pragmatist governance and illustrating their practicality the aim is to make plausible the claim that the new search networks

are in principle governable, but not to suggest that they are already well governed. On the contrary: Leaving aside cases of egregious financial wrongdoing, it is striking that there is not a single, generally recognized example of sustained, organized, and well characterized good governance in a multinational firm, including of course the many indisputably successful ones. Worse yet, many, if not all, the cases of corporate governance of innovation that have been presented as exemplary soon proved seriously defective.

Reality check—graph on current governance mess

Final word on the hope for democracy in the revolt against routine. No one should believe that democracy is about to be reborn just because there is pervaise pressure to redistribute "improvisation" rights. But only a congential pessimist can be unmoved by the possibility that the deepest fundaments of our despair about democracy and self determination are being quietly shaken by a revolution in organized problem solving.

NOTES

1 See below, p.

2 John Dewey, Human Nature and Conduct, is careful to distinguish habit, as the creative disposition to respond, almost unselfconsciously, to new situations on the basis on long experience, from routine, as habit frozen into a compulsion to repeat prior responses despite novelty in the situations that typically trigger them.

3 For examples of how NUMMI (the GM-Toyota joint venture) handles the tension between standard operating procedures and continuous improvement, see Adler et al, 1999.

4 Weick, Sutcliffe, and Obstfelf

5 Schoen, D. A. "Generative Metaphor: A Perspective on Problem-Setting in Social Policy", in Metaphor and Thought. Ortony, A., ed. New York: Cambridge University Press, 1979. pp. 254-283, pp. 257-259.

6 Simon, The Science of the Artificial, pp. 90-92.

7 See Herrigel's essays, and his interview with ITW officer. Notice that in casting about for an organizational solution to the innovator's dilemma of managing "sustaining" or routine lines of business without being blindsided by "disruptive" threats, Christensen seizes on the example of a company—Nypro—whose structure is similar to ITW's, but whose governance procedures are in crucial ways less formal and effective. What ITW is to metal components and small systems, Nypro is to plastics: a federation of many small units providing specialized products in various industries. Nypro, like ITW provides central research and development services to its largely independent business units. The key difference is that Nypro has no equivalent to ITW's 80/20 dis-entrenching rule. Instead the firm uses periodic meetings

among unit managers to spread ideas and develop a cooperative culture despite their rivalry for the headquarters' approval. In addition the CEO keeps close touch of innovations that diffuse among several units, and requires that the most successful of these be incorporated into the firm's standard operating procedures. There are, however, no systematic incentives, as there are at ITW, to scrutinize present practices for clues about new markets. This, for Christensen, remains the job of the CEO. (innovator's Solution, 271-275, "institutions can't disrupt themselves" is from p. 274)

8 Mayer, David, and Kenney, Martin F. "Economic Action Does Not Take Place in a Vacuum: Understanding Cisco's Acquisition and Development Strategy," BRIE Working Paper 148September 16, 2002, esp. p. 24 for the account of the "make or buy" review.

9 See US Department of Agriculture, Food Safety and Inspection Service, 9CFR Part 304, et al. Pathogen Reduction; Hazard Analysis and Critical control Point (HACCP) Systems; Final Rule, Federal Register, Thursday, July 25, 1996, 38805-38850.

10 For the limits to the current implementation of the HACCP, see Petersen, Melody, and Drew, Christopher, "New Safety Rules Fail to Stop Tainted Meat," New York Times, Oct 10, 2003. pg. A.1. But for an illustration of the ways this system produces the information needed to pinpoint deficiencies it its own implementation, see US Department of Agriculture, Office of Inspector General, Great Plains region Audit Report, Food Safety and Inspection Service Oversight of Production Process and Recall at Conagra Plant (Establishment 969), rep[ort No. 24601-2-KC, September 2003.

Charles Sabel

Maurice T. Moore Professor of Law and Political Science
at Columbia University

PROCEDURALISATION AND POLYCENTRIC REGULATION

Julia Black [1]

INTRODUCTION

In an article which prompted my invitation to this conference,[2] I noted that procedures and institutional structures which facilitated participation were being advocated to address a range of perceived regulatory problems, from the 'big picture' issues of globalisation, the rise of the risk society, and the failures of the steering state, to the more mundane issues of telecommunications regulation, corporations and insolvency law, and environmental regulation. These calls echo with those writers in regulation who are both advocating and observing the rise of the 'new regulatory state'[3] or even the 'post-regulatory'[4] state in which the state moves from the direct regulation of behaviour to the adoption of indirect techniques, a move which Scharpf has described as 'social gardening' rather than 'social engineering'.[5]

As I noted in that paper, proceduralisation is a term which is used to encompass both the basket of new techniques of regulation which characterize or are prescribed for the 'post' regulatory state including enhanced participation, and the quite particular technique, advocated by Teubner, of changing organisational processes so as to ensure internal democratization and external responsiveness. It was on this latter meaning that my article focused. The two facets of this is latter meaning of 'proceduralisation': democratisation and responsiveness, are clearly linked, but it is on democratisation that the argument was centred. In a critique of Teubner I argued that advocating internal democratisation and external responsiveness could not take the form, as Teubner argued, of a 'mere' technique of regulation devoid of any substantive values. At the very least, one had to be able to identify

which of its 'consequences' a system had to be responsive to and how much responsiveness was enough. More particularly, one also had to ask which conception of 'democratisation' was being advocated, in particular was it a model of liberal democracy, or of a more complex and more demanding model of deliberative democracy. If it was the former, this would be a fairly 'thin' form of proceduralisation: the extension of egoistical voting beyond the institution of the legislature or political elections. If the latter, this would be a 'thick' form of proceduralisation, and moreover would have strong resonances with Habermas's theory of deliberative democracy and procedural law, resonances made all the stronger by Teubner's own engagement with Habermas's work, in particular a shared focus on the changing and multiple roles of law as an instrument and expression of forms of contemporary governance.

In considering Habermas's conception of deliberative democracy and procedural law I argued that his theory posited a concept of the state and of regulation that was over-centred on the classic triumvirate of the legislature, executive and judiciary, and invoked a distinction between politics and the life-world that is too clear cut. Habermas's main acknowledgement of the changing face of contemporary governance is to extend his requirements of deliberation to the administration. But this is woefully inadequate for those who argued that in order to understand the nature of contemporary governance the focus of attention has to be shifted from the state to non-state actors who interact with each other and the state in varied and complex ways. This conception of regulation as 'decentred'[6] 'multi-centred'[7] or 'nodal'[8] challenges any theory of governance which focuses predominantly on the state. They have particular relevance for Habermas, given his reliance on the institutions of the state to provide the conditions for the attainment of deliberative democracy, and to act as 'sluices' which 'cleanse' the multiple deliberations of the public sphere as they pass through.[9]

The article further argued that even where deliberation can be injected into the regulatory system, there are a range of difficulties to be overcome. Many of these are well noted in the extensive literature on deliberative democracy, and my article focused on just one: how to ensure communication between participants who did not share a communicative rationality. Facilitating communication in these circumstances, I argued, required, amongst other things, strategies of translation and dispute resolution. 'Social gardening' deliberative democracy style would require regulators to move from being bureaucrats to diplomats. In considering the ability of regulators to pursue these strategies, the article was pessimistic, arguing that regulators, particularly state regulators, were not best placed to perform these roles for a range of reasons: depending on the distribution of decision making authority, they would rarely, if ever, be in the position of true mediators, and moreover their own communicative rationalities may impede their ability to understand another's, let alone translate it.

The article also ended with two questions: in what aspects of the regulatory system and in what stages of the regulatory processes can we realistically 'inject' deliberation or participation of either a thick or a thin form, and to what extent are some or all of the techniques of procedural regulation or the 'post' regulatory state compatible with the substantive aspect of 'thick' proceduralisation?

This paper takes those two questions as its starting point, but refines them slightly. First it sets them more firmly in the context of decentred understandings of regulation. Secondly, it focuses on only one set of techniques, those related to enforcement. As such it omits many other issues, but pleads the benefits of brevity and the demands of time.

The first part of the paper briefly outlines what it being referred to by 'decentred' approaches to regulation, arguing that if we adopt a perspective which displaces the state from the centre of a regulatory system, the polycentricity of regulation is more clearly revealed. The second part outlines some of the implications of taking a decentred approach for how we understand and perhaps develop regulatory systems as enrolling the differential regulatory capacities of actors to perform different regulatory functions, in ways which move us far beyond the simple dichotomy of statutory versus self regulation. In the third part it is suggested that as a consequence of adopting the perspectives of decentred regulation and enrolment, we can see more clearly not only the fragmented nature of regulatory processes, but also the potential 'entry' points for democratization or at least participation in different regulatory functions. In other words, we do not have to see regulation as an activity which to be effective is or has to be performed by hierarchical bureaucracies acting in accordance with formal rationality. The fourth section then uses examples from enforcement processes to illustrate how this may be achieved, and what some of the 5 preconditions for success might be, before in the final part asking how these examples can be used to develop further ideas of 'constitutionalising' polycentric regulation.

Decentred understandings of regulation

'Regulation' as a social and political activity is universal; however the term 'regulation' is not one that travels well, and those who have attempted to study regulation outside English-speaking countries will be aware there is often no parallel term. So in order to at least set the parameters of the debate, 'regulation' here is used to mean a sustained and focused attempt by state or non-state actors to alter the behaviour of others which is otherwise valued as useful to society with the intention of producing a broadly identified outcome or outcomes, which may involve mechanisms of standard-setting, information-gathering and behaviour-modification.[10] This is not to say that outcomes may result that were other than those that were

intended, simply that the activity of regulation is a purposive one, even if the purposes achieved are not those intended, or indeed that no purposes are achieved at all. Most importantly, however, no particular institutional or organisational arrangement is assumed in the definition, neither are particular techniques. Regulators may operate at a transnational, supranational, national or sub-national level, and boundaries between regulator and regulated might shift. Both regulators and the regulated may be governments, formal or informal associations, firms, individuals, and play other roles: professional advisors, accreditors, auditors, non-governmental organisations, charities, voluntary organisations, and so on.

The core understanding that many have of 'regulation' is some form of 'command and control' (CAC) regulation: regulation by the state through the use of legal rules backed by (often criminal) sanctions. 'CAC' has also however become shorthand to denote all that can be bad about regulation, including poorly targetted rules, rigidity, ossification, under- or over- enforcement, and unintended consequences. The extent to which CAC does or does not live up to this caricature is an empirical question which has been debated elsewhere.[11] More importantly for this discussion, CAC regulation posits a particular role for the state against which the 'decentring' analysis is counterposed. It is 'centred' in that it assumes the state to have the capacity to command and control, to be the only commander and controller, and to be potentially effective in commanding and controlling. It is assumed to be uni-lateral in its approach (governments telling, others doing), to be based on simple cause-effect relations, and to envisage a linear progression from policy formation through to implementation. Its failings are variously identified as including the following: that the instruments used (laws backed by sanctions) are inappropriate and unsophisticated (instrument failure), that government has insufficient knowledge to be able to identify the causes of problems, to design solutions that are appropriate, and to identify noncompliance (information and knowledge failure), that implementation of the regulation is inadequate (implementation failure), and that those being regulated are insufficiently inclined to comply, and those doing the regulating are insufficiently motivated to regulated in the public interest (motivation failure and capture theory).

As noted, many discussions of CAC regulation to an extent set up a straw man, which can easily be knocked down. Nonetheless, there is a set of alternative perspectives on the nature of governmentsociety, and intra-society interactions which posits a more decentred conception.[12] These writings have both descriptive and prescriptive aspects. They share neither the assumptions nor the diagnosis of the 'centred' analysis of regulation, and embrace a far wider set of techniques than the 'rules backed by sanctions' of CAC regulation. The main intellectual influences are Foucauldian inspired analyses of governance,[13] and systems theory, particularly as filtered through Teubner, though for many the intellectual roots are more pragmatic.[14]

A decentred conception of regulation has five central notions: complexity, fragmentation, interdependencies, ungovernability, and the rejection of a clear distinction between public and private.

Complexity A decentred understanding of regulation emphasises both causal complexity and the complexity of interactions between actors in society (or systems). There is an increasing recognition that social problems are the result of various interacting factors, not all of which may be known, the nature and relevance of which changes over time, and the interaction between which will be only imperfectly understood. More conceptual writings also draw attention to the dynamic interactions between actors and / or systems, and to the operations of forces which produce a constant tension between stability and change within a system (loosely defined). Those interactions are themselves complex and intricate, and actors are diverse in their goals, intentions, purposes, norms and powers.[15]

Fragmentation refers to fragmentation of knowledge, and fragmentation of power and control. The fragmentation of knowledge is more radically formed than the more familiar problem of the information asymmetry between regulator and regulated: that government cannot know as much about industry as industry does about itself. In a decentred understanding of regulation, it is not assumed that any one actor has all the information necessary to solve social problems: it is not a question of industry having, government needing. Rather, no single actor has all the knowledge required to solve complex, diverse and dynamic problems, and no single actor has the overview necessary to employ all the instruments needed to make regulation effective. The problem is sometimes more radically framed to be that not only is knowledge fragmented but that information is socially constructed - there are no such things as 'objective' social truths. This conclusion is arrived at via various theoretical routes, most influential in regulatory writings has been autopoeisis. Autopoietically closed sub-systems, such as politics, administration and law, construct their images of other subsystems only through the distorting lens of their own perceptual apparatus, that is through experiences of their environment and in terms of their own binary oppositions. Thus the information systems possess about other systems is simply that which they have themselves constructed in accordance with their own criteria.16 The conclusion is also reached through various strands of new institutionalism, discourse theory, cultural theory and some decision making theories: that is that decision makers, organisations, etc, construct images of their environment in their own image, or through their own cognitive frames.17

Decentring analyses also draw on Foucauldian notions of power to emphasis that in addition to fragmentation of knowledge there is fragmentation of power and control. Government does not have a monopoly on the exercise of power and control. Rather it is dispersed between social actors and between actors and the state.[18] Moreover, as many have observed, the regulatory systems existing within social

spheres are seen as equally, if not more, important to social ordering as the formal ordering of the state. Regulation occurs in many locations, in many fora; there is 'regulation in many rooms'.[19]

Autonomy and ungovernability Observations of fragmentation relate to the third central aspect of a decentring analysis, and that is the autonomy and ungovernability of actors (or systems). Autonomy is not used in the sense of freedom from interference by government, rather it is the idea that actors will continue to develop or act in their own way in the absence of intervention. Actors or systems are self regulating, and regulation cannot take their behaviour as a constant. Regulation is, as Foucault said of governance, the 'conduct of conduct',20 or as re-phrased by Rose, 'to act upon action'.21 This has several implications, first and most obviously that regulation will produce changes in behaviour and outcomes that are unintentended (though not necessarily adverse), a well recognised empirical phenomenon in regulation.22 Second, that its form may have to vary depending on the attitude of the regulatee towards compliance, an attitude which it can itself affect, again recognised in practice in regulatory literature.23 Third, that no single actor can hope to dominate the regulatory process uni-laterally as all actors can be severely restricted in reaching their own objectives not just by limitations in their own knowledge but also by the autonomy of others,24 a clear counterpoint to the assumptions of theories of 'regulatory capture'. Whether that is because of the actors' capacity to employ power and resources for action,25 or because of the inherent characteristics of the system, or for some other reason, is a moot point. Fifthly, that the autonomy of the actor will to an extent render it insusceptible to external regulation. Here, autopoiesis has the more radical analysis of autonomy. Autopoeticists diverge on the meaning of autonomy, but broadly it refers to the self-regulation, self-production and self-organisation of systems which are normatively closed but cognitively open.26 The consequence: that no system can act directly upon another. Attempts to do so will result in Teubner's well known regulatory trilemma: the indifference of the 'target' system to the intervention, the destruction of the 'target' system itself, or the destruction of the intervening system.27 Finally, that subjects or systems have the capacity to regulate themselves, a capacity that has to be harnessed for 'government at a distance' to be effective.

Interactions and interdependencies A decentring analysis has as part of its core the existence and complexity of interactions and interdependencies between social actors, and between social actors and government in the process of regulation.28 Regulation is a two-way, or three or four-way process, between all those involved in the regulatory process, and particularly between regulator and regulatee in the implementation of regulation. In Offe's terms, regulation is 'co-produced'.29 However the relationship is not seen to be one in which society has needs (problems) and government has capacities (solutions). Rather each is seen as having both

problems (needs) and solutions (capacities), and as being mutually dependent on each other for their resolution and use.30 These interactions and interdependencies should not be presumed to be contained within national territorial borders: analyses of globalisation emphasise that they may extend well beyond them.

Rejection of the public / private distinction In decentred analyses, regulation 'happens' in the absence of formal legal sanction - it is the product of interactions, not of the exercise of the formal, constitutionally recognised authority of government.31 The collapse of the public / private distinction as a useful tool for analysing governance and regulation is manifested in the identification of 'hybrid' organisations or networks that combine governmental and nongovernmental actors in a variety of ways. To the governing alternatives of bureaucracies (hierarchies) and markets have been added associations - the 'private interest governments' identified by Streeck and Schmitter which comprised the new corporatism. The concept of authority still played a role, however, for these organisations shared in the state's authority to make and enforce binding decisions'.32 Added more recently are networks: the interactions of a range of actors, of which the state is only one, and which it has been argued government both does use and should use to govern.33 Governance, and regulation, is seen by some to be the outcome of the interactions of networks, or alternatively 'webs of influence' which operate in the absence of formal governmental or legal sanction.34 In a decentred understanding of regulation, therefore, formal de lege authority plays an ambiguous role.

There are four main implications of a decentred perspective on regulation. First, it suggests a diagnosis of regulatory failure which is based on the dynamics, complexity and diversity of economic and social life, and in the inherent ungovernability of social actors, systems and networks. Secondly, regulation is revealed to be polycentric, or multi-nodal: to occur in many forums which are often interrelated in complex ways, and in ways which belie a clear dichotomy between 'state' and 'self' regulation. Even in predominantly state based systems of regulation, non-state actors will be involved at various sites in ways that are not apparent if an approach is adopted which centres only on the state, and conversely predominantly 'self' regulatory systems may involve many different relationships with the state and with other non-state regulators.

Thirdly, there is a set of prescriptions as to the types of regulatory strategies that should be adopted which is tied more or less loosely to this conceptual base. The hallmarks of these decentred strategies are that they are hybrid (combining governmental and non-governmental actors), multifaceted (using a number of different strategies simultaneously or sequentially), and they are indirect.[35] The diagnosis of regulatory failure provided by the decentring analysis suggests that regulation should be a process of co-ordinating, steering, influencing and balancing interactions between actors / systems, and of creating new patterns of interaction which enable

social actors / systems to organise themselves, using such techniques as proceduralisation, collibration, feedback loops, redundancy, and above all, countering variety with variety.[36] The impetus for many of these prescriptions comes from autopoiesis: the functional differentiation of society into cognitively closed, normatively open self referential systems, though analyses of the tools of regulation to be employed may only be weakly attached to this particular theoretical base. In most instances, discussion occurs in the context of how the state should design regulatory mechanisms in order to achieve its objectives, and indeed some have been labelled as the strategies of the 'new regulatory state'.[37] The role that the state plays in any of them will range from full participant to mere guiding hand or threatening shadow. The decentring analysis suggests however that similar forms of strategies will have to be used whether or not the state is present at all, even in ghostly form.

Fourthly, it is worth noting that there is less consensus on the particular normative goals that should be achieved in using such strategies. For many, the goal of regulation is the project of welfare economics: the correction of market failure, and traditional conceptualisations of 'regulation' have assumed it to be an activity directed principally towards that objective (and correspondingly, anything that was not so directed was not 'regulation'). In the standard treatments of 'regulation', the 'why regulate' question is nearly always answered in terms of the correction of market failures, with the occasional nod to distributional or other ancillary aims.[38] However, that goal is being displaced, and others added. Notably, the management and distribution of risk: regulating the 'risk society' is a burgeoning academic and policy area and there are signs that existing systems of regulation, for example UK financial services, are coupling the correction of market failure with the management of risk as their organising principles. Other goals which it is argued regulation should pursue, in particular by those coming from a socio-legal base, are access to justice,[39] or legitimacy,[40] or the achievement of social justice in some form.[41] Alternatively, normative goals are sometimes framed functionally as in Teubner's version of system's theory, in which the normative goals of regulation must be to create the conditions for responsiveness, to prevent the entropy or self destruction of systems, and to stimulate system integration.[42] Whether those normative goals are confined to systems of regulation in which the state is involved, or whether they extend to regulation conducted by all social actors (assuming we can extend 'regulation' beyond the state), is an equally contentious debate, which is addressed further below.[43]

Regulatory actors, capacities and enrolment

Decentred analyses of regulation may resonate with sociologists of regulation, but they are potentially problematic for policy makers. They emphasise complexity and fluidity over simplicity and predictability and give a complex and thick description

of a regulatory system which provides little succour for those who seek to regulate, be that the state or another actor.[44] The notion of regulatory enrolment is simultaneously an attempt to provide an analytical framework which can facilitate the description and understanding of contemporary regulation and which can form the basis of critiquing the system, and an attempt to provide some help to those who seek to regulate in recognition of this complexity and fluidity.[45] It has five main elements, which are interrelated. These are the disaggregation of what regulation entails in functional terms, the identification of actors who are or might be involved in the regulatory system, an analysis of their regulatory capacity, relating that capacity to different regulatory functions, and an analysis of the interrelationships that arise between the actors in the regulatory system.

Disaggregating regulatory functions

Cybernetics, various strands of which have been increasingly influential in writings on regulation in law and political science, suggests that there are three core functions that have to be performed in order to 'regulate' something, and these have to be performed in an on-going, dynamic process.[46] These are setting standards, gathering information on the current state of behaviour including the attainment of standards, and modifying behaviour. Interpreted narrowly, this cybernetic disaggregation of regulation does not tell us very much that we did not already know. In particular, it runs the risk of simply redescribing CAC regulation: regulation involves forming rules, monitoring compliance and ensuring enforcement, either through negotiation or the imposition of sanctions or some combination of the two.[47] To avoid this, we need first to broaden our conceptions of these functions to include identifying problems and goals, as well as writing rules, and to broaden methods of behaviour modification beyond modes of enforcement, and secondly to recognize the interrelationship between the three elements: ways in which information is gathered, for example, will affect both how problems and goals are identified, and how behaviour is modified (eg speed cameras).

Identifying actors

In identifying actual or potential regulatory actors we need to move away from the bald categories of state, market, associations and individual regulated firm, and indeed from the dichotomy of state vs self-regulation, and to consider in more detail, and more systematically, who the different actors might be and how they might (or might not) be inter-connected. The range of actors may include governmental and non-governmental associations at the international, national and subnational level; market actors (eg those further up the supply chain); gatekeepers or persons who control key resource that firms need, for example credit ratings agencies, insurers, auditors, internet service providers; advisors, for example legal,

management, risk and IT consultants, accountants and other 'knowledge intermediaries'; competitors and professional counterparties; community and voluntary associations; charities; consumers; the regulated firm and individuals within the firm, including compliance officers, front line personnel and CEOs; influential individuals, eg 'policy entrepreneurs' and 'grey panthers'; and the courts.

Regulatory resources and regulatory capacity

So far, so familiar. The analysis needs to go further if we are to progress in understanding how regulation is or could be constituted. What is suggested is an analysis of the regulatory capacity of different actors to perform different regulatory functions and consideration of how they are or might be enrolled within a regulatory system.

Regulatory capacity has no clearly agreed definition and any discussion is clearly going to be in answer to the implicit question: capacity to do what? Here the question is, who has the capacity, alone or in combination with any other, to perform all or any of the regulatory functions effectively both now and in the future in such a way that furthers the (conflicting) purposes of those seeking to regulate and which is normatively acceptable.

Regulatory capacity, it is suggested, is a composite notion, consisting of the actual or potential possession of resources plus the existence of actual or potential conditions that make it likely that those resources will be deployed both now and in the future in such a way as to further the identified goals of those seeking to regulate resolve identified problems, however vague and contradictory those might be.[48] It consists thus not just of the possession of resources but the ability and willingness to use them.

Any assessment of what resources are necessary to perform a regulatory function is likely to vary at the detailed level with the particular context. However, it is suggested that distilling from the literature on the operation of regulatory systems, six key resources can be identified as being critical to the performance of at least one or more regulatory functions. These are: information, expertise, financial and economic resources, authority and legitimacy, strategic position, and organisational capacity. An actor might possess a resource directly, or indirectly in that it might have access to the resources of others. An actor may also be a resource for others. For example, the fact that a particular actor is requiring a certain form of conduct might provide leverage to another actor who is better placed to affect the relevant behaviour. Thus a regulator may be a resource for a compliance officer: the fact that an enforcement official is coming down hard on a regulated firm might give a compliance officer the leverage she needs to ensure that management take the issue seriously.[49] Or a private sector advisor (eg management consultant) may be a resource for a regulatory official or manager within a firm seeking to implement internal management changes.[50]

Information

It is well recognised that information is a key resource for all regulatory functions. Information on which to base policy decisions, as well as information how the potential targets of regulation act, interact and are likely to react, is indispensable to the formation of standards and the development of techniques of behaviour modification, and information has to be timely, relevant and reliable, or at least have the potential to be made reliable. That is equally true of a state or national regulator as it is of a firm, of an industry association, or indeed a parent. But as the decentring analysis emphasises, any single actor is likely to have only part of the information necessary. National regulatory bodies often have information on levels of implementation and compliance in its own jurisdiction, but not in others; or macro-level data but not micro-level.[51] 'Non-scientific' knowledge and experience can be vital in developing effective risk regulation regimes. [52] One of the arguments for involving non-state associations in deliberations on policy is to enhance the information available.[53]

Expertise

Expertise is a critical regulatory resource as expert discourses have a critical role in defining issues, patterning organisational structuring and control, and mediating between governmental policies and their implementation.[54] Expertise can thus be an important source of power. [55] In a regulatory context this is manifested in the domination of particular conceptualisations of problems at different times, and how certain definitions of problems or potential solutions open up issues such that they become seen as the preserve of many participants or potential participants, or conversely close them down, defining them as the preserve only of particular groups of 'experts'.[56] For the conflict may be not only in the conflict of lay versus expert discourses,[57] or economic versus non-economic discourses,[58] but between expert discourses as to which dominates. For example, the debate relating to the patenting of human genetic sequences is characterized by the competing discourses of law, biology, ethics and economics.[59]

Authority and legitimacy

Authority and legitimacy are also well-recognised as key resources contributing to the capacity to regulate.[60] The two are separate but interconnected. By authority is not meant necessarily legal authority, thought that might be the form that it takes. Rather by authority is meant whether or not what an actor says or requires makes a 'practical difference' to the way that others act or behave, and whether it does so simply by virtue of the actor saying it. In other words, does the mere fact that a particular actor stipulates that a particular course of conduct should be followed mean that others (though by no means all) will alter their conduct not as a result of a rationalistic pursuit of preferences but principally out of a sense of obligation, or because that actor is respected or esteemed within the community for whatever reason.[61]

Legitimacy is a distinct but related resource, and serves a dual role in the analysis. First, there is a relationship between legitimacy and effectiveness. Second, the possession (or not) of legitimacy is a normative as well as an empirical assessment - including legitimacy as an element of regulatory capacity thus provides a normative dimension to the analysis. Again, by legitimacy is not meant whether or not an actor has the legal power to act. Rather is meant whether or not an institution or organisation is perceived as having a 'right to govern' both by those it seeks to govern and those on behalf it purports to govern.[62] The perceived possession of this right may be based on a wide range of criteria: the representativeness of an organisation, for example, or the nature of its procedures, its legal mandate, its efficiency, its expertise, its effectiveness.[63] That criteria is likely to vary with a range of different audiences, leading often to a legitimacy paradox. In other words, there may be many 'legitimacy communities', ie communities whose legitimacy criteria may be quite opposed.

Strategic position

Strategic position is by its nature a relative concept: the question is, does the actor occupy a key position vis a vis the ultimate target of the regulation. For example, does the actor possess a resource that the target needs or desires, such as finance or access to a market, or indeed trust or respect.[64] By definition, 'gatekeepers' are those that possess a strategic position. [65] The resource might be financial, knowledge-based, or it may be something more intangible, for example credibility or trust, acceptance and respect.[66]

Organisational capacity

Much of the work on enforcement of regulation concludes that the reason that both negotiative and deterrence compliance strategies fail is due to lack of organisational capacity to comply, rather than being related to lack of willingness to comply or rational calculation to non-comply.[67] Weaknesses in organisational capacity have also been identified as a critical problem in regulating small and medium enterprises.[68] Organisational capacity refers in part to the ability to handle complex technical problems,[69] but may be extended to the ability to solve problems more broadly,[70] and the ability to learn.[71] It also refers to the capacity of an organisation to regulate its own internal affairs, and thus for the organisation itself and for those actors charged with regulatory functions within it (including management functions) to have the resources above and to deploy them within their organisation.

Deployment of resources and changes in capacity over time

As noted, however, resources are only one element of regulatory capacity. What is equally as important is how those resources are being or are likely to be used. In addressing this issue, institutionalist literature suggests a range of factors that are likely to be relevant.[72] These may be divided for ease of exposition into two sets,

internal and external factors. External factors include the legal environment, the economic and market context, the institutional / organisational context, and the political and social context.[73] Internal factors mean the actor's interests, preferences and thus their incentives, whether those are seen as exogenously formed as in economic analyses, or formed endogenously as in sociological analyses: their values, perceptions, ideas, 'culture', 'worldview' or 'cognitive frame'. In other words, the way they see the world and their place in it, how problems are defined, and what are considered to be appropriate solutions. [74] Moreover, organisations are not 'black boxes'. Instead they have 'multiple selves': different individuals and groups within organisations are likely to have quite different interests and quite different mind sets, which may operate in tension with one another. Which becomes dominant is likely to be the result of a complicated process of the deployment of power and institutional position.

Finally, as regulatory capacity is likely to change over time, and possibly rapidly, an important element in assessing regulatory capacity is the likelihood of any change, its probable direction, and its likely consequences.[75] Indeed, changes in regulatory capacity might themselves be the intended or unintended outcome of strategies of enrolment. For example, a market actor who currently provides information to the market about a firm might be enrolled in the regulatory process in that the information might be used as a formal part of the government regulatory assessment of that firm: environmental audits are one example, another from financial services is the use rating agencies' assessments of credit worthiness of banks in assessing capital adequacy requirements. However, the fact that the information becomes used for such a purpose may itself introduce a new set of incentives for both firms and rating agencies, which in turn may lead to inaccurate or partial information being given, which then negates the effectiveness of the regulatory strategy. An important element in the assessment of regulatory capacity is thus the resilience of that capacity: in other words, how susceptible the capacity is changes in resources and in internal and external factors, and what the implications are for the success of the enrolment strategy in different scenarios of change.

Enrolling actors in regulatory processes

Different resources are valuabl e for different regulatory functions, with the result that certain actors may be well-placed to perform some regulatory functions but not others.[76] If an actor could combine in some way with another actor that possesses a different configuration of regulatory capacity then the capacity of both could be increased.[77] This potential for interconnections to increase overall capacity can be overlooked; rather complex sets of interrelationships such as networks are usually criticised, often rightly, by public lawyers and others for blocking publicly optimal

governance or regulation, or for obscuring lines of accountability. Nonetheless, the significance of interlinkages in enhancing regulatory and governance capacity has long been noted in the governance literature[78] and in the literature on the sociology of control,[79] and has recently entered the more mainstream regulatory literature.[80] Sometimes described as 'webs',[81] more frequently as 'networks', the significance of such interlinkages is that they enhance the capacity of any one actor to achieve its goals. Much of the analysis stems from Granovetter's seminal argument on the 'strength of weak ties'.[82] In other words, that linkages between actors that are relatively weak in terms of mutuality, time, and degree of reciprocity may nonetheless serve a cohering function, and the more an individual is embedded in a network of weak ties, the more their capacity for action may be enhanced.[83] This may be used by individuals to their strategic advantage: Callon and Latour for example define power as the ability of any one actor to enrol others to achieve that actor's aims.[84]

Although the term 'enrolment' can conjure up images of networks, enrolment as understood here does not necessarily imply that the actors exist in a network relationship (ie patterns of interrelationships that involve a variety of actors each pursuing their own goals, between whom there are relatively stable sets of inter-relationships, and critically, who are dependent on one another for resources)[85] nor does it imply that this is an unqualifiedly superior form of arrangement to other types of inter-relationship. Moreover, it should be noted that who is enrolled and who is doing the enrolling is a matter of perspective. From the perspective of a compliance officer in a firm, for example, he or she may seek to enrol a regulator (be it a trade association or statutory regulatory agency or some other actor) to bolster his or her own authority within the firm; however from perspective of the association or agency it is enrolling the compliance officer in the task of modifying the behaviour of others within the firm. Moreover, the strategy of enrolment may be used consciously or unconsciously, implicitly or explicitly, and may occur without any changes in formal rules or the formal distribution of power or functions. Furthermore, relationships of enrolment or assessments that 'X is enrolling Y' do not necessarily mean that X will succeed in ensuring that Y will act in the way that X is anticipating or hoping they will act. Enrolment does not mean the end of unintended and unforeseen consequences, nor is it to be assumed (as the Chicago school assume) that the enrolled actor is simply a cipher for the aims and objectives of the enroller.

Finally, there are a number of dimensions to enrolment, and thus a number of perspectives that may be used to analyse the form it takes. Enrolment may be analysed by looking at the nature of the inter-relationship between actors, but also by looking at the function that an actor is being enrolled to perform, the resources that are being enrolled, and the character of the enrolment (formal or informal, iterative or random / ad hoc), and these dimensions may be considered individually or in any combination.[86]

Implications of the decentred analysis and regulatory enrolment for democratization / proceduralisation

The argument thus far has been first, that analyses of regulation should adopt a decentred perspective, which will reveal the polycentricity of regulation and the multiple and shifting roles that different actors play in a regulatory process. Secondly, that the activity of regulating requires actors to have regulatory capacity, in other words to have access directly or indirectly to particular resources and have the willingness to deploy those resources for regulatory ends. Different resources are differently valuable for different regulatory functions, so different actors will be more or less able to perform those functions. Further, enrolling actors with differential regulatory capacities in regulatory processes can enhance the regulatory capacity of the system as a whole. Finally, understanding those patterns of enrolment can help us better to understand how regulatory processes work, and provide a basis for how they can be improved against a range of criteria, including legitimacy.

It is on this latter point that the remainder of the discussion will focus. It was argued above that legitimacy is a key regulatory resource; moreover including legitimacy as a resource gives the analytical framework a critical edge: to what extent are actors involved in the regulatory process who do not possess legitimacy? As noted above, criteria for legitimacy are likely to be contested, which will always ensure this question has a complex answer. In the following argument, the criteria for 'legitimacy' will be taken to be the degree of to which the requirements of thick proceduralisation, or deliberative democracy, are met by the actor / forum in which regulatory activities are being carried out (eg of the standard setting body, or a firm or other association involved in the regulatory system). This is clearly not the only criteria of legitimacy, even for constitutional legitimacy, for that embraces other values: compliance with the rule of law, transparency, accountability, due process and so on. But it will serve to focus the argument for the moment.

Decentred analysis and notions of regulatory enrolment, it is suggested, can assist us in the quest for greater proceduralisation or democratization of regulation because they emphasise fragmentation both of the process of regulation and of the range of actors involved. Fragmentation and complexity is usually criticized for obfuscating accountability or the application of constitutional values such as democratization, often with good reason. Multiple actors performing multiple roles means not only many entry points but many veto points, a high potential for policy incoherence and endless opportunities for blame-shifting and evasion of responsibilities, as any observer of UK railways regulation will agree. But there is a potential upside to decentred analyses, which is that 'mapping' regulation in ways which reveal its polycentricity (or multi-nodality) and which highlight the different ways in which multiple actors are enrolled in those processes can help us break down the question of how and where democratization, or other desired constitutional values, can be

inserted into the process. For if we are to make progress in improving the responsiveness of contemporary regulation to these values we need to think at a detailed and micro level. We cannot ask 'how can regulation be made responsive to democracy / the rule of law / procedural fairness / pursuit of justice as nondomination' and expect either a simple answer or one which would be relevant to every regulatory system. We have to start from the bottom up – how can this regulatory process, or even this part of this process, be made responsive to those values?

In beginning to answer this question, I suggest that it is helpful to go back to the different regulatory functions and to pose the question: how can this function be democratized, or more broadly, constitutionalised?

This question is most often posed with regards to the first identified regulatory function: setting policies and objectives, including the determination of rules or principles (either legal or nonlegal). It is with regards to this issue that most of the focus on widening participation and democratization occurs: what should we as a society identify as a problem and what should we do about it. In turn, the argument is how can we democratize those who are making decisions on these issues, be they the international standard setting organizations of the WTO, IMF, or other intergovernmental organizations, technical standard setting bodies, national or subnational legislators or executive bodies, or even corporations. However, there are other regulatory functions, notably information gathering and modifying behaviour. As noted above, some of the work on deliberative democracy which focuses on the role of associations in decision making emphasizes the significant informational advantages of including a wider range of participants in the formation of policies, principles and rules.[87]

It is on the third, related aspect of the regulatory function that I want to focus here, however, and that is behaviour modification, for two reasons. First, it occupies the 'black box' usually labelled 'implementation', which is usually ignored in the broader debates on democratization. Emphasising implementation is not to deny the inevitable and continuing interrelationship between policy formation and implementation; rather it is to emphasise that the focus is on everything that occurs once the legislation has been passed, principle agreed to or standard set. For there is always a danger that even if the initial stages of establishing the regulatory principles there was a high degree of deliberative democratization there will thereafter be a gradual process of incremental exclusion of participants, leaving only conversations between regulator and regulated; what rational choice institutionalists would term 'coalitional drift'.[88] Secondly, focusing on this aspect of regulation brings us back to the question posed at the start, which is what the relationship is between different regulatory techniques and proceduralisation: what would 'deliberative democratic techniques' of regulation take the form of, even assuming it is apposite to talk of deliberative democracy in terms of a regulatory technique?

It is clear that some regulatory techniques are not at all deliberative in their operation, particularly those which are based on what Lessig calls 'architecture'.[89] These involve no deliberation or even conversational interactions in the way that they modify behaviour (though considerable deliberation is possible in their design). Bentham's pentopticon is the most famous theoretical example of this technique. Milder examples are the spaces which are designed in such a way as to ensure that people move in particular directions; these modify behaviour without any conversational interaction between the regulator (here the person who designed the space, though for some the space itself) and the regulated (the person walking through).[90] Studies in policing have shown the importance of the design of public spaces for preventing crime.[91] Using architectural techniques for crowd control can be a major aspect of health and safety regulation. For example, in the London Underground there are always more escalators bringing people out of the station than there are taking them in, to limit the numbers waiting on the platforms at any one time (on the rare occasion the escalators are working at all). Lessig provides another example: the design of computer software ensures that I take certain actions not others, or have access to only certain parts of cyberspace or not others. The spacing of barriers in the road next to customs posts can effectively inhibit 'ramming' of customs checks without any need for deliberation between driver and customs official.[92] These techniques, it should be noted, are particularly interesting as they differ from other non-discursive techniques, such as road signs, traffic lights, speed cameras, not so much in that they offer me less choice of whether or not to comply, but that they place physical and not simply normative barriers in the way of my non-compliance.

Other techniques involve a comparatively high degree of conversational interaction, particularly the most common technique of regulation by rules or principles.[93] Indeed, regulatory conversations are a central feature of most regulatory systems. By regulatory conversations I mean the communicative interactions between regulators, regulated and others involved in the regulatory process concerning the operation of that regulatory system, including interpersonal communications, documents, guidance notes, policy briefings, seminars, conferences and so on.[94] I distinguish regulatory conversations from deliberation in the sense the latter is used in deliberative democratic theory, as conversations do not necessarily conform or even aspire to the conditions of the ideal speech situation.

In particular, regulatory conversations are a central feature of systems of regulation based on written norms. Written norms are central to a wide range of regulatory techniques: they form a core part of regulatory techniques or combinations of techniques including the various forms of self regulation, meta-regulation, competition, associational or procedural regulation, and are the basis of many 'economic' tools of regulation such as taxes, subsidies and instruments such as tradeable permit systems, as well as franchising, licensing and audit regimes. Written norms have

two central features which make them particularly problematic regulatory instruments: their temporal aspect, they speak from the past or present but purport to govern the future, and their linguistic aspect: they are linguistic structures which require interpretation. How they will 'work' depends on the interpretation they receive. Regulatory conversations about the prescriptions for the conduct necessary to resolve particular problems and the meaning and application of those prescriptions in particular circumstances are likely to be a central feature of those regulatory systems that employ them, though they are often likely to be closed conversations between regulator and regulated.[95] Further, particular techniques of regulation are themselves based on conversational interactions: proceduralisation itself, and strategies of co-regulation, negotiated regulation, even models of corporate social responsibility, all emphasise deliberation as a central feature of the regulatory technique, not simply a by-product of it.

Further, regardless of the techniques employed to modify behaviour, regulatory conversations are likely to be a central characteristic of the regulatory process where the task of regulation is uncertain and ambiguous, and where agreement on the definitions of problems and solutions presupposes an extensive inter-subjective sharing of ideas and negotiations of meaning. Regulation of risk provides an obvious example; but conversations will also be important in the more general situation in which regulators are given broadly defined and conflicting objectives to fulfil or principles to follow, where they operate in a dynamic context in which problem definitions are complex and shifting, and the consequences of regulatory action uncertain.

To the extent that regulatory conversations are already a central part of many regulatory techniques, they may be more or less open to thick proceduralisation in principle (ie they have the potential in theory to be democratized in the sense required by deliberative democracy albeit in practice this may not be realized. As noted above, it is difficult to make generalizations on this issue: what is necessary is a more fine-grained consideration of how proceduralisation can occur in the different regulatory functions and in different regulatory locations.

Proceduralising enforcement processes: lessons from restorative justice

In choosing to focus on the behaviour modifying aspects of regulatory systems, one could look at the entire basket of regulatory techniques, clearly a significant task. Instead, I focus here on just one: enforcement. Enforcement is clearly a significant part of any regulatory process, but here I do not confine enforcement to mean the application of civil or criminal sanctions by a court. Rather the focus is on those instances where the regulatory requirements have been breached, and those whose role it is to respond to breaches have chosen to do so (for not all breaches of regulation

are responded to, even though they are known about). How they choose to respond remains an open issue, and clearly the line between action that is labelled monitoring and that labelled enforcement is a fluid one. Moreover, whilst examples from state-based regulation are drawn on here, the approaches discussed need not be, and indeed are not, confined to state-based systems of regulation.

In the UK at least, the traditional mode of enforcement for regulatory offences in state-based systems is criminal prosecution and / or the application of civil sanctions by a court, and / or administrative sanctions usually involving fines and / or remedial plans by regulatory agencies. Those involved in determining the sanction to be imposed are the institutions of the court or agency, and participation in those decisions is limited to the offending firm and their legal advisors, although the regulatory agency might have a disciplinary panel whose membership embraces a wider range of stakeholders (eg worker, consumer or practitioner representation). Enforcement actions by non-state regulators often include financial penalties and exclusion.

Democratising the enforcement process in regulation has not received nearly the same attention as democratizing the processes of policy formation and norm-setting. Moves have been made in this direction by John Braithwaite, however, who has argued that regulation could and should learn from the experience of restorative justice in the enforcement of criminal law.[96] Restorative justice processes, ideally, are about restoring victims, offenders and communities, where what is to be restored is whatever it is that is important to those groups, to be deliberatively determined by those 'stakeholders' in any particular circumstance, that is by the offender, the regulator and the victim.[97] As Braithwaite continues to elaborate throughout the book, restorative justice is a group process of polycentric problem solving which often requires the definition of the issues to be broadened well beyond the offence itself, which incorporates the principles and practices of reintegrative shaming, and which empowers affected communities to deal with the consequences of injustice and tranform private troubles into public issues.

It is not, however, an entirely subjective process which is impervious to external assessment: what the parties agree is not necessarily acceptable just because they have agreed it. In this respect Braithwaite seeks to escape from the normative paradox of deliberative democracy, though he does not interact with that literature. Public accountability of restorative justice processes is also critical in ensuring the publicisation of what might otherwise remain private processes of justice, and can thus help to avoid one of the feminist critiques of ADR and mediation processes. Restorative justice, in Braithwaite's model, should be evaluated in terms of its effectiveness at promoting respect for fundamental human rights as enumerated in various international statements on human rights, and more particularly at the restoration of values including human dignity, property loss, personal injury, damaged human relationships, communities, the environment, emotional restoration, freedom,

compassion or caring, peace, empowerment or self-determination and a sense of duty as a citizen.[98] It should not however have as its primary objective the promotion of apology, mercy and forgiveness, on the basis that these should only be given voluntarily or they will be worthless. Creating spaces in which they might be forthcoming is an appropriate objective; mandating them is not.[99] Further, restorative justice processes should be constrained by the principles of republican justice[100] and more particularly by rights that are fundamental to liberal conceptions of the rule of law.

Research on restorative justice processes is at present mainly confined to criminal justice processes, not regulation. However, Braithwaite argues that the principles of restorative justice can be, and have been, manifested in regulatory processes. He seeks to marry his conception of restorative justice with his model of responsive regulation, developed with Ayres.[101] Responsive regulation is a strategy of regulation in which regulators respond to the conduct of those they seek to regulate in deciding whether a more or less interventionist response is required. The 'regulatory pyramid' which Braithwaite developed with Ian Ayres has become an established feature of the regulatory literature. The pyramid is a set of regulatory enforcement and sanctioning tools of increasing punitiveness and severity; the strategy of responsiveness is that in deploying these tools regulators start at the bottom of the pyramid, with persuasion, working their way up only if the regulatee's response is non-co-operative at each successive stage. The critical element is that the escalation should be seen to be inexorable and credible, and as organisationally and procedurally quite separate from the bottom level, ie out of the personal control of the particular enforcement officer dealing with the firm.

What responsive regulation provides restorative justice with is an institutional structure in which the consequence of not following the voluntary restorative justice processes or honouring its principles is an escalation of interventionism and sanctioning. In other words, in the criminal justice context the legal process will take over, with all the increased sanctions, costs etc that that entails. What restorative justice gives responsive regulation is a practical and normative framework for what should occur at the bottom rung of the pyramid. That is, that the process of persuasion should not simply take the form of a closed dialogue between firm and regulator, but should be broadened to include wider stakeholders, notably victims, and should encompass the key elements of the restorative justice process including reintegrative shaming and stakeholder restoration.

In one striking example, Braithwaite illustrates the potential of restorative justice approaches to enforcement to democratise the process, and to deliver responses from the firm for its behaviour which mirrored the polycentric nature both of the issues and, I would argue, involved the enrolment of a range of regulatory capacities of actors within the regulatory system. In the mid 1980s, a number of insurance companies in Australia were implicated in defrauding consumers through misrepresentations

about policies sold to them. In the case of one company, Colonial Mutual Life (CML), the worst abuses occurred in twenty two remote Aboriginal communities. [102] Once the breaches were discovered, the regulatory agency instructed top management from the insurance companies to visit the communities. They in fact had quite lengthy visits, meeting victims, local Aboriginal community council, the regulators, local officials at the social security department where premiums were being deducted from social security benefits, and some executives went back deeply ashamed of what had occurred. Meetings were then held in Canberra with insurance regulators and industry associations and even the prime minister about follow up regulatory reforms. The plurality of participants led to an agreement with CML which voluntarily compensated 2000 policy holders, and CML funded the Aboriginal Consumer Education Fund to 'harden targets' for future attempts to rip off illiterate people. It conducted internal investigation into its compliance programme and to identify those responsible. Press conference was then called to reveal enormity of the problem. Over 80 individuals were sacked in the firm, including some senior managers, and one large corporate agent dismissed. Procedures for welfare checks were changed at the social security department and there were regulatory and self regulatory changes concerning licensing of agents and changes to the law. Restorative justice thus led to polycentric problem solving, and in the terms of the framework set out above, recognised the various roles of a range of different actors, enrolling their regulatory capacities within the regulatory system.

Christine Parker has argued that the use of enforceable undertakings in Australian trade practices law can be characterised as an example of restorative justice.[103] Enforceable undertakings are, as their name suggests, undertakings entered into by the firm to conduct remedial actions which are agreed in negotiation with the regulator, and that agreement is legally enforceable with sanctions attaching for its breach. The ACCC uses enforceable undertakings in cases where there is evidence of a breach of the regulatory requirements as an alternative to prosecuting or taking civil action. Agreeing an undertaking does not require an admission of liability from the firm, but it is the ACCC's policy not to use undertakings where the firm denies liability. Parker reports that the undertakings typically include, firstly, a positive commitment by the alleged offender to cease the alleged misconduct and not recommence it, secondly, provisions for compensation, reimbursement or redress to affected parties, and other corrective action as appropriate (eg corrective advertising); thirdly a requirement to implement a compliance program and to have the implementation of that program independently reviewed, and finally, though less frequently, the enforceable undertaking may also include requirements that the Commission calls 'community service orders' such as funding or implementing an industry or consumer compliance education program. She characterizes the practice of determining enforceable undertakings as a form of 'restorative justice' and argues

that properly structured, and when nested within a pyramid of credible and more onerous regulatory sanctions, they can meet criticisms of both fairness and bias whilst delivering innovative, flexible and expansive undertakings that go beyond what a court would order with the purpose of identifying, correcting and preventing the original breach and its underlying causes.

Parker uses the example of how 'telephone slamming' was dealt with by the ACCC in 2000 to illustrate how restorative justice processes are being used in regulation.[104] 'Slamming' refers to deceptive door-to-door sales tactics and telemarketing methods that result in customers' services being illegally (ie without legitimate authorisation) transferred from one service provider to another. Once the CEOs became aware of the evidence the ACCC had of how egregious the conduct of their agents had been, and the fact that their companies would be liable for that conduct, the case was settled by enforceable undertaking and admissions to the court. In the undertakings the companies agreed to notify all customers acquired during the relevant period of the breaches that had occurred and to invite them to make contact if they felt they had been affected. They also agreed to consider all complaints and, where they found that a transfer was not authorised, to reverse the transfer if the customer wished, and reimburse all payments made by the customer during the relevant period, or not seek payment for services provided during that period. Finally the enforceable undertakings included provisions for the telecommunications companies to review not only their own compliance programs but their selling channels and methods and arrangements for transfer, with the result that most moved the bulk of their marketing from direct sales to telemarketing, over which they could exercise greater control. In addition the relevant trade association drafted a new customer transfer code addressing all the issues raised in the ACCC investigation, and the telecommunications and marketing companies agreed to donate substantial sums to fund education programmes for consumers, a programme designed by the trade association in consultation with ACCC and consumer groups.

These examples are drawn from state-based systems of regulation. However there is no reason why restorative justice style processes need be confined to such systems. Braithwaite uses the examples of the treatment of bullying in schools to show how democratisation of the decisions of how to respond to breaches in desired standards of behaviour together with the 'conference technology' of restorative justice circles can result in 'whole school' responses to the problem which provide, he argues, 'better' outcomes on a range of criteria than more closed, dyadic processes or the immediate use of sanctions without any prior negotiation (ie moving too fast up the enforcement pyramid).[105] He also draws on Rees's work on the development of selfregulatory systems for the regulation of the safety of nuclear power installations in the wake of Three Mile Island which involve extensive peer review and participation in inspections as an example of how 'restorative justice' approaches can

deliver outside of state-based systems of regulation. Parker has shown similar results in the way that breaches of sex discrimination rules are dealt with in firms.[106]

The work on restorative justice is highly pertinent for debates on the proceduralisation or democratization of regulation, simply because it advocates a democratic mode of decision making in the exercise of a key regulatory function: enforcement. Moreover, it accords with 'thick' conceptions of proceduralisation for although it does not draw closely on the theoretical underpinnings of deliberative democracy, it clearly has strong resonances with it and could be 31 sited without much difficulty in that theoretical framework. Moreover, many of the criticisms leveled at restorative justice processes (domination, stigmatization, role of facilitators and so on) are also leveled at deliberative democracy processes. In answering these, Braithwaite exhibits much of the same optimism as those who are committed to public reason in deliberation, and shares Habermas's conviction that consensus can and will be reached on key moral issues in society. He also offers some useful prescriptions, based on empirical evidence, of how deliberations should be structured to facilitate participation. He proposes that the 'technology' of conferencing in restorative justice is superior to dyadic negotiations on the one hand between victim and offender, and direct democracy on the other, as it involves circles of participants who are specifically invited on the basis of their relationship with the offender and the victim: so helping to meet the problem of domination and stigmatization on the one hand, and failure to participate on the other.

However, even if we accept Braithwaite's defence of restorative justice and share his pathological optimism in its potential,[107] there are three difficulties which are faced in simply 'enrolling' restorative justice processes into regulatory systems to enhance their democratization. First, it is clear from the evidence reviewed that deliberative processes of enforcement are only effective when nested within a set of credible sanctions. There still needs to be a big stick somewhere: these can be found in non-state systems, one might just have to look harder; alternatively the nonstate system may in some cases be able to enrol state systems of sanctions to provide it with the necessary clout. The need to find a stick, though, suggests a limit to the effectiveness of deliberative processes on their own to deliver desired regulatory outcomes, in this case changes in behaviour and remediation, in circumstances where the force of the better argument is insufficient, and where the potential for reneging on any agreement reached is high.

The second issue is that the examples that both Braithwaite and Parker draw on to illustrate how restorative justice has been introduced into regulatory systems may be deliberative between those who are involved, but the set of participants is limited to the firm and the regulator. The victim is often excluded, as are wider groups of stakeholders In excluding the victims the examples they draw on do not always meet their own criteria for restorative justice, and in doing so perhaps implicitly

reveal the limit to which limit to which restorative justice processes as used in criminal justice can be directly transposed into regulatory settings.

Victim involvement in restorative justice processes in the criminal context occurs in two main decisions: whether restorative justice processes should be used at all, and what the 'restoration' is that should be made. However in all the examples Braithwaite and Parker give of the use of restorative justice in regulatory contexts it has been the regulator who has the authority to decide whether or not to impose a sanction that has the authority to decide whether a restorative justice enforcement process will be used. Further, whilst in some of the examples that they cite of restorative justice in regulation do include direct participation by victims or representative victim groups (eg Aboriginal communities in the CML case above, and involvement of residents' committees in determining responses to breaches of nursing home regulation), other examples (eg telephone slamming) do not include victim participation in the decision, although they do involve compensation being paid to victims.

Thus whilst their examples are excellent case studies in imaginative and targeted responses to regulatory breaches, which recognise the polycentricity of the problem and involve the enrolment of the regulatory capacities of a range of actors to perform different types of regulatory function, one has to ask to what extent they are all examples of restorative justice, or at least of the 'democratisation' of the enforcement process. For example, in the case of telephone slamming at no point were the victims involved in the deliberations as to what remedial and compensatory actions should be taken. And indeed, there are a number of features characterising the victims which suggest that their involvement would not be as straightforward as in the CML case. Victims were a diffuse group, considerable numbers were involved, but the loss in each case was relatively small. Moreover, they were not easily identifiable to the telecommunications companies themselves, nor would the victims easily be aware of the fact they were victims. It is hard to get victims to participate when noone knows who they are. This is not a facile comment: in a similar exercise in the UK relating to pensions misselling, one of the main obstacles to awarding compensation to victims of misselling was trying to identify who those victims were. This was partly because identifying whether or not a person had suffered a loss involved complex actuarial calculations (though in practice these were short circuited in the pensions review and it was simply assumed that certain classes of people would have been worse off). It was also because companies simply did not have adequate records of who they had sold policies to, and victims had no idea that they might have been missold.[108]

There are ways in which these problems could be addressed: victims' action groups can participate, for example, are often quick to form once a problem has been adequately publicised in the media, providing at least an example of the spontaneous

action of the public sphere)), though there are always issues about the representativeness and internal democratisation of any representative group. The point is not that the lack of victim involvement illustrates an implicit and insurmountable problem, it is rather that the examples these authors draw on to illustrate how restorative justice has been introduced into regulatory processes do not make their case as well as they could, because critically they lack victim involvement at the two points in the process that restorative justice models demand it. They also mean that the discussion of restorative justice in regulation glides over an issue which is dealt with in great detail in the context of criminal justice, and that is, who should participate in the deliberations, how wide should the net be cast, and how can their participation be managed.[109]

The third issue points to the potential for the deliberations in restorative enforcement processes to reach agreement, and to meet the requirements of the ideal speech situation. Braithwaite argues restorative justice works best where all agree that an action is morally wrong, as this can facilitate an appeal to higher loyalties.[110] For, drawing on Habermas, he argues that the closer we get to conditions of undominated speech, the more overwhelmingly it will be the case that evils such as violence will be nearly universally condemned. Indeed he sees this as a virtue: 'a nice moral feature of restorative justice. is that restorative justice might work only with crimes that ought to be crimes.' So, for example, he argues restorative justice would not work to deal with cases of obscenity as participants may dispute whether obscenity should be a crime. He does not see this as a problem, however, as he argues that 'most criminal offenses brought to justice in democratic societies are more like the violence case than the obscenity case: they are unambiguously wrong to most citizens attending conference.'[111] However this is not the case in regulation. The distinction usually drawn between criminal law and regulation is that the latter is directed at behaviour which is not seen as valuable in a community, whereas the former seeks to modify behaviour which is otherwise seen as valuable. As a result, perhaps, regulation is fraught with moral ambivalence: where is the moral force in environmental law, or financial services law, or consumer protection? Indeed, the moral ambivalence of regulation has been explained as influencing compliance processes in other contexts.[112] One is likely to have many who will dispute whether the regulatory provision is valid at all: appeal to higher loyalties, and thus to a different communicative rationality, is unlikely to work quite so well. Moreover, the need for translation will arguably be higher, though little is said on how this can be achieved.

It should not be surprising that some of the most intractable problems of deliberative democracy remain unresolved by restorative justice processes, particularly as the latter are still in their infancy. Nonetheless, it is suggested that the restorative enforcement processes can be used to illustrate the broader argument that this paper is making, which is that if we disaggregate the regulatory process we can begin to

see more clearly which aspects of it can be proceduralised in particular cases. It is through this micro-level approach, in which the polycentricity of regulatory processes is recognised and the multiplicity of actors and the variety of regulatory capacities analysed, that we can make more progress in the debates on proceduralising polycentric regulation.

Conclusion: Proceduralisating and Constitutionalising Regulation

This paper has sought to address two questions: assuming we adopt a decentred analysis of regulation, in what aspects of the regulatory system and in what stages of the regulatory processes can we realistically introduce deliberation, and to what extent are some or all of the techniques of procedural regulation or the 'post' regulatory state compatible with the substantive aspect of 'thick' proceduralisation? It has argued that adopting a decentred perspective on regulation reveals its polycentricity, and that using the analytical framework of regulatory capacity and regulatory enrolment can facilitate a more nuanced and fine-grained understanding of a regulatory system. This in turn can help us to identify potential 'entry' points for proceduralisation, for the introduction of deliberation. In addition, it has suggested that some regulatory techniques may be more amenable to proceduralisation or democratization than others. Some techniques, notably those based on spatial architecture, are not based on communicative interactions for their implementation and operation, and so 'proceduralising' them makes no sense. Most other techniques, however, do involve regulatory conversations, and thus there might in certain cases be the potential for those to be democratized. The paper has addressed one set of techniques, those relating to enforcement, to examine how democratization could be realized in practice.

Throughout the paper, the focus has been on 'thick proceduralisation' or the introduction of deliberative democratic processes into regulatory systems. Proceduralisation is only one normative goal, however. It may be that we do not want deliberative democracy (because, for example, we doubt the benefits of consensus in regulation)[113] or that we despair of ever attaining it. This does not preclude the need for other constitutional values to be applied to polycentric regulation, such as due process, transparency, predictability or proportionality. The key question for patterns of contemporary governance is how these broader constitutional values, not just those of deliberative democracy, can be met, given that many of the actors are non-state bodies, to whom these constitutional principles have not always applied. It is suggested that in order to progress in this debate we need to look at the micro-level, at specific situations, and that by using the analytical perspectives of decentring and regulatory enrolment we can begin not only identify more clearly where different constitutional values need to be introduced, and how this can be achieved.

NOTES

1 Reader, Law Department and research member, ESRC Centre for the Analysis of Risk and Regulation, London School of Economics and Political Science. This paper was written whilst on research leave funded by the ESRC, and I thank them for their support.

2 J. Black, 'Proceduralising Regulation: Part I' (2000) 20 *Oxford Journal of Legal Studies* 597-614 and 'Proceduralising Regulation: Part II' (2001) 21 *Oxford Journal of Legal Studies* 33-59.

3 J. Braithwaite, 'The New Regulatory State and the Transformation of Criminology' (2000) 40 *British Jnl of Criminology* 222; C. Parker, 'Reinventing Regulation within the Corporation: Compliance Oriented Regulatory Innovation' (2000) 35(2) *Administration & Society* 529; C. Parker, *The Open Corporation: Self-Regulation and Corporate Citizenship* (Cambridge: CUP, **).

4 G. Teubner, 'Substantive and Reflexive Elements in Modern Law' (1983) 17 *Law & Soc Rev* 239; J. Black, 'Decentring Regulation: Understanding the Role of Regulation and Self Regulation in a "Post-Regulatory" World' (2001) 54 *Current Legal Problems* 103-147.

5 G. Teubner, 'Regulatory Law: Chronicle of Death Foretold' (1992) 1 *Social and Legal Studies* 451, 463, quoting F. Scharpf, 'Grenzen der institutionellen Reform' (1987) *Jahrbuch zur Staats und Verwaltungswissenschaft* 111.

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8 C. Shearing and J. Wood, 'Nodal Governance, Democracy and the New 'Denizens" (2003) 30(3) *Journal of Law and Society* 300.

9 See also J. Cohen and C. Sabel, 'Directly-Deliberative Polyarchy' (1997) 3 ELJ 313; and M. Dorf and C. Sabel, 'A Constitution of Democratic Experimentalism' (1998) 98(2) Col LR 267.

10 J. Black, 'Critical Reflections on Regulation' (2002) 27 *Australian Journal of Legal Philosophy* 1.

11 See R. Baldwin. 'Regulation: After Command and Control' in K. Hawkins (ed), *The Human Face of Law* (Oxford, 1997); N. Gunningham and P. Grabovsky, *Smart Regulation: Designing Environmental Policy* (Oxford, 1998), 38-50.

12 There is no single exposition of a 'decentred understanding', but central to the analysis developed above are the following writings: G. Teubner (ed), *Juridification of the Social Spheres* (Berlin, 1987); . G. Teubner (ed), *Dilemmas of Law in the Welfare State* (Berlin, 1986). G. Teubner and A. Febbrajo (eds), *State, Law, Economy as Autopoietic Systems* (Berlin, 1992); G. Teubner, L. Farmer and D. Murphy, *Environmental Law and Ecological Responsibility* (London, 1994); R. Veld et al, *Autopoiesis and Configuration Theory: New Approaches to Societal Steering* (Dordrecht, 1991); in the governance literature: M. Foucault, 'Governmentality' in G. Burchell, C. Gordon and P. Miller, *The Foucault Effect: Studies in Governmentality* (London, 1991); N. Rose and P. Miller, 'Political Power Beyond the State: Problematics of Government' (1992) 43(2) *British Journal of Sociology* 173; N. Rose, *Powers of Freedom* (Cambridge, 1999); J. Kooiman (ed), *Modern Governance: New Government-Society Interactions* (London, 1993); N. Rose, 'Government and Control' (2000) 40 *British Jnl of Criminology* 321; R. Rhodes, *Understanding Governance* (Buckingham, 1997). The spirit of decentring is also evident in writings in criminology, see eg D. Garland, *The Culture of Control* (Oxford, 2001).

13 Particularly the work of Niklas Rose.

14 Eg Rhodes.

15 Kooiman,

16 See Teubner.

17 See eg); P. DiMaggio and W. Powell 'Introduction' in W. Powell and P. DiMaggio, *The New Institutionalism in Organisational Analysis* (1991), M. Foucault, 'Politics and the Study of Discourse' in G. Burchell, C. Gordon and P. Miller, *The Foucault Effect* (Hemel Hempstead, 1991); M. Schwarz and M. Thompson, *Divided we Stand* (Hemel Hempstead, 1990); K. Hawkins and P. Manning, 'Legal Decisions: A Frame Analytic Perspective' in S.H. Riggins (ed), *Beyond Goffman: Studies on Communication, Institution and Social Interaction* (Berlin, 1990).

18 Foucault, 'Politics and the Study of Discourse'; Rose and Miller; C. Gordon, 'Governmental Rationality: An Introduction' in Burchell et al (eds).

19 See eg L. Nader and C. Nader, 'A Wide Angle on Regulation: An Anthropological Perspective' in R. Noll (ed), *Regulatory Policy and the Social Sciences* (Berkely, Calif., 1985)

20 See Foucault, 'Politics and the Study of Discourse'; Gordon, 'Governmental Rationality'.

21 Rose, (1999), 4.

22 See eg P. Grabovsky, 'Counterproductive Regulation' (1995) 23 *Int. J. of Sociology of Law* 347.

23 See eg R. Kagan and J. Scholz, 'Regulatory Enforcement Strategies' in K. Hawkins and J. Thomas, *Enforcing Regulation* (Boston, Mass., 1984), R. Baldwin, *Rules and Government* (Oxford, 1995), D. McBarnet and C. Whelan, 'The Elusive Spirit of the Law: Formalism and the Struggle for Legal Control' (1991) 54 MLR 848.

24 J.Kooiman, 'Governance and Governability: Using Complexity, Dynamics and Diversity' in J. Kooiman (ed), , 44-47.

25 See eg Mayntz who argues that highly institutionalised and organised subsystems may resist political control, but argues that it is not their self referential closure which makes intervention difficult but the actions of identifiable actors in resisting intervention / creating autonomy by employing the power resources and capacities for collective action characteristic of highly organised societal sectors: R. Maytnz, 'Governing Failures and the Problem of Governability: Some Comments on a Theoretical Paradigm' in J. Kooiman (ed), , 17.

26 See G. Teubner, *Law as an Autopoietic System* (Oxford, 1993), 32-34.

27 G. Teubner, 'Juridification: Concepts, Aspects, Limits, Solutions' in Teubner (ed), n. 4 above (1987).

28 See eg J. Kooiman, 'Findings, Speculations and Recommendations' in J. Kooiman (ed), , 253; Rhodes, n.4 above, 50-59; Rose, n. 4 above, ch 1; L. Hancher and M. Moran, 'Organizing Regulatory Space' in L. Hancher and M. Moran (eds), *Capitalism, Culture and Economic Regulation* (Oxford, 1989).

29 C. Offe, *Contradictions of the Welfare State* (London, 1984),.310; J. Black, 'Talking About Regulation' (1998) Public Law 77.

30 Kooiman, above.

31 Rhodes, n.* above.

32 P. Streeck and P. Schmitter, 'Community, Market, State - and Associations? The Prospective Contribution of Interest Governance to Social Order' in P. Streeck and P. Schmitter (eds), *Private Interest Government: Beyond Market and State* (London, 1985), 20.

33 See eg Rose, n. * above, 16 et seq

34 Rhodes, n. * above, J. Braithwaite and P. Drahos, *Global Business Regulation* (Oxford, 2000).

35 Eg Teubner, n. * above and related analyses.

36 References at n. * above.

37 Braithwaite, n. * above; C. Parker, 'Reinventing Regulation within the Corporation: Compliance Oriented Regulatory Innovation' (2000) 35(2) *Administration & Society* 529; C. Parker, *The Open Corporation: Self-Regulation and Corporate Citizenship*.

38 Eg S. Breyer, Regulation and its Reform (Harvard, 1982); A. Ogus, *Regulation: Legal Form and Economic Theory* (Oxford, 1994), R. Baldwin and M. Cave, *Understanding Regulation* (Oxford, 1999).

39 C. Parker, *Just Lawyers* (Oxford, 1999).

40 Baldwin and Cave, n. * above; R. Baldwin, *Rules and Government* (Oxford, 1995).

41 I. Ayres and J. Braithwaite, *Responsive Regulation* (Oxford, 1992).

42 Teubner, nn.4 and 18 above; G. Teubner, 'Substantive and Reflexive Elements in Modern Law' (1983) 17 Law & Soc Rev 239.

43 For an argument on the 'horizontality' as well as 'verticality' of rights and obligations see eg J. Habermas, *Between Facts and Norms* (transl. 1999).

44 C. Scott, 'Accountability in the Regulatory State' ** Public Law **, 352.

45 The discussion in this section draws on J. Black, 'Enrolling Actors in Regulatory Processes: Examples from UK Financial Services Regulation' [2003] Public Law 62 and J. Black, 'Mapping the Contours of Financial Services Regulation'.

46 C. Hood, *Tools of Government* (London, Macmillan, 1983); Hood et al, n.* above; C. Hood, H. Rothstein and R. Baldwin, *The Government of Risk: Understanding Risk Regulation Regimes* (Oxford: OUP, 2001); Scott, n.* above; Scott and Murray, [MLR].

47 Eg Hood, Rothstein and Baldwin, pp.23-27; whilst they discuss the alternative enforcement techniques that might be used (compliance vs deterrence strategies), there is little suggestion of other forms of behaviour modification, and in particular how the alternatives to CAC might fit into the descriptions of the control functions as set out there.

48 For an alternative understanding of regulatory capacity see L. Stirton and M. Lodge, 'Embedding Regulatory Autonomy: The Reform of Jamaican Telecommunications Regulation 1988-200, CARR Discussion Paper No. 4 (London: LSE 2002), available at http://www.lse.ac.uk/depts/carr.

49 For examples of this type of activity, and indeed of compliance officers asking enforcement officers to act in a more 'sanctioning' manner to enable them to achieve just this effect, see C. Parker, *The Open Corporation: Self Regulation and Corporate Citizenship* (Cambridge: CUP, forthcoming).

50 Saint-Martin, for example, argues that management consultants increase the capacity of public officials charged with implementing reform helping them to overcome bureaucratic resistance: D. Saint-Martin, *Building the New Managerialist State* (Oxford, OUP, 2000), 198.

51 See eg Hall and Soskice, *Varieties of Capitalism* **.

52 B. Wynne, 'Where Sheep May Safely Graze' **.

53 Cohen and Sabel

54 Eg the role of epistemic communities in the policy process: P. Haas, 'Introduction: Epistemic Communities and International Policy Co-ordination' (1992) 46(1) *International Organisation* 1; P. Haas, 'Obtaining International Environmental Protection through Epistemic Consensus' in I.Rowlands and M. Greene, *Global Environmental Change and International Relations* (1992); P. Haas, 'Epistemic Communities and the Dynamics of International Co-operation' in V. Rittberger and P. Mayer, *Regime Theory and International Relations* (1993); P. Miller and N. Rose, 'Governing Economic Life' (1990) 19 *Economy and Society* 1. In the regulatory context see M. Hajer, *The Politics of Environmental Discourse*

(Oxford: OUP, 1995) and for general discussion J. Black, 'Regulatory Conversations' (2002) 29(1) JLS 163.

55 See references at n. * above, Hall, , Knorr-Cetina,.

56 Hajer.

57 For a good overview see Royal Society, *Risk: Analysis, Perception, Management* (1992).

58 Eg B. Morgan, *Social Citizenship*.. **.

59 J. Black, 'Regulation as Facilitation: Negotiating the Genetic Revolution' (1998) 61 MLR 621

60 See for example Scott, n.* above, Baldwin and Cave, n.* above; J. Black, 'Talking About Regulation' (1998) Public Law 77.

61 The concept thus draws on the concept of authority developed in jurisprudence by Raz as elaborated by Coleman: J. Raz, *The Authority of Law* (Oxford: OUP, 1979); J. Coleman, 'Incorporationism, Conventionality and the Practical Difference Thesis' *The Practical Difference Thesis* (1998) 4 *Legal Theory* 381.

62 See discussions in R. Barker, *Political Legitimacy and the State* (Oxford: OUP, 1990).

63 For discussion see R. Baldwin and J.C. McCrudden, *Regulation and Public Law* (London: Weidenfeld and Nicholson, 1987); and Baldwin and Cave, n.* above.

64 Trust and respect, for example, are key resources in the implementation of Braithwaite's theory of restorative justice: Braithwaite, n* above; id., *Crime, Shame and Reintegration* (Cambridge: CUP, 1989).

65 See references at nn.* above.

66 On the role of trust and respect in governance and restorative justice see respectively Sharpf,; Braithwaite,.

67 See eg I. Ayres and J. Braithwaite, *Responsive Regulation* (Oxford: OUP, 1992).

68 For discussion see N. Gunningham, 'Regulating Small and Medium Sized Enterprises' (2002) 14 *Jnl Environmental Law* 3.

69 M. Grindle, 'The Good Government Imperative: Human Resources, Organisations and Institutions' in M. Grindle (ed), *Getting Good Government: Capacity Building in the Public Sector of Developing Countries* (Cambridge, Mass: Harvard Institute for International Development, 1997); Stirton and Lodge, n.44 above.

70 Eg Sparrow, *The Regulatory Craft* .

71 See eg K. Weick and F. Westley. 'Organizational Learning: Affirming an Oxymoron' in S. Clegg, C. Hardy and W. Nord, *Handbook of Organization Studies* (London: Sage, 1996).

72 For a review of its application in the regulatory context see J. Black, 'New Institutionalism and Naturalism in Socio-Legal Analysis: Institutionalist Approaches to Regulatory Decision Making' (1997) 19 *Law and Policy* 51.

73 On the latter see N. Gunningham [CARR Discussion Paper].

74 For discussion of the importance of such factors in the regulatory context see for example E. Meidinger, 'Regulatory Culture: A Theoretical Outline' (1987) 9 Law & Pol 355; K. Hawkins and P. Manning, 'Legal Decisions: A Frame Analytic Perspective' in S. Riggins, *Beyond Goffman: Studies on Communication, Institution and Social Interaction* (de Gruyter, Berlin, 1990); P. Selznick, *The Moral Commonwealth: Social Theory and the Promise of Community* (1993); Hall, Scott and Hood, n.51 above.

75 For further discussion and examples see J. Black, 'Mapping the Contours of Contemporary Financial Services

Regulation' (2002) 2 Journal of Corporate Law Studies.

76 See Black, 'Enrolling Actors in Regulatory Processes'.

77 The embeddedness of actors is a key element of regulatory capacity in Stirton and Lodge's analysis: n.* above.

78 In sociology and governance see Rose and Miller, , Rose,; N. Rose, *Powers of Freedom: Reframing Political Thought* (Cambridge, 1999); in political science / public administration and governance see eg R. Rhodes, 'Power-dependence, Policy Communities and Intergovernmental Networks' (1985) 49 *Public Administration Bulletin* 4; id, n.* above; Jordan, n.* above; id., 'Policy Community Realism vs 'New' Institutionalist Ambiguity' (1990) 38 *Political Studies* 470; D. Marsh and R. Rhodes (eds), *Policy Networks in British Government* (Oxford: OUP, 1992); D. Marsh (ed), *Comparing Policy Networks* (Buckingham: Open University Press, 1998); D. Marsh and M. Smith, 'Understanding Policy Networks: Towards a Dialectical Approach' (2000) 48 *Political Studies* 4.

79 Eg J. Law (ed), *Power, Action, Belief: A New Sociology of Knowledge?* (London, 1986); J. Law and J. Hassard, *Actor Network Theory and after* (Oxford: Blackwell Publishers, 1999).

80 Braithwaite and Drahos, n.* above; Stirton and Lodge, n.* above.

81 eg Braithwaite and Drahos, ibid.

82 M. Granovetter, 'The Strength of Weak Ties' (1973) 78(6) Am J Sociol 1360.

83 For discussion in a regulatory context see eg Stirton and Lodge, n.* above.

84 M. Callon and B. Latour, 'Unscrewing the Big Leviathan: How Actors Macro-Structure Reality and How Sociologists Help them to do so' in K. Knorr-Cetina and A.V. Cicourel, *Advances in Social Theory and Methodology: Toward an Integration of Micro- and Macro-Sociologies* (London: Routledge, 1981).

85 Sharpf, n.* above; J. Benson, 'A Framework for Policy Analysis' in D. Rogers and D. Whetten (eds), *Interorganizational Coordination: Theory, Research and Implementation* (Ames: Iowa State University Press, 1982); Gage and Mandell (eds), n.* above; E-H. Klijn, 'Policy Networks: An Overview' in Kickert, Klijn and Koopenjan, n.* above.

86 For further discussion and examples see Black, n.* above.

87 Above n.*.

88 eg McNollGast; Macey.

89 Lessig, Code; see also C. Hood, *Tools of Government* (**)

90 Shearing, Disney World

91 Garland

92 Sparrow, Regulatory Craft.

93 Black, Talking about Regulation' [1997] Public Law **; Black, 'Regulatory Conversations'.

94 J. Black, *Rules and Regulators* (1997), J. Black, 'Talking about Regulation' (1998) Public Law 77 and J. Black, 'Regulatory Conversations'.

95 Black, Rules and Regulators.

96 J. Braithwaite, *Restorative Justice and Responsive Regulation* (Oxford: OUP, 2002); and that restorative justice can learn from responsive regulation.

97 RJRR, 11.

98 RJRR 14-15.

99 Ibid.

100 Developed in J. Braithwaite and P. Pettet, *Not Just Deserts: A Republican Theory of Criminal Justice* (OUP, Oxford, 1990)

101 I. Ayres and J. Braithwaite, *Responsive Regulation* (Oxford: OUP 1992).

102 RJRR, 23-4; Fisse and Braithwaite 1993, p.235.

103 C. Parker, 'Restorative Justice in Business Regulation? The Australian Competition and Consumer Commission's use of Enforceable Undertakings' (2004) *Modern Law Review* (forthcoming, March 2004).

104 Parker, 'Enforceable Undertakings'.

105 Ref ch 4

106 ref ch 4

107 RJRR, 137.

108 J. Black and R. Nobles, 'Personal Pensions Misselling: The Causes and Lessons of Regulatory Failure' (1997)* *Modern Law Review* **.

109 For example, there may be a case for extending participation to include members of the firm's peer group. One of the critical elements in restorative justice is to structure the conference so as to include representatives from all the different segments of an offender's life: to merge roles that the offender might otherwise want to separate (RJRR, 87). Involving firms' or others whose respect the CEOs of the offending firm respect could be a valuable addition to a restorative enforcement process.

110 RJRR, 88.

111 RJRR, 88.

112 K. Hawkins, *Environment and Enforcement* (Oxford: Clarendon Press, 1984), *.

113 Eg C. Coglianese [**]

Julia Black

READER, LAW DEPARTMENT AND RESEARCH MEMBER,
ESRC CENTRE FOR THE ANALYSIS OF RISK AND REGULATION,
LONDON SCHOOL OF ECONOMICS AND POLITICAL SCIENCE

DELIBERATION, INTERESTS AND PLURALISM? *

Fábio W. Reis

I

If we are concerned with democracy, then *autonomy* is a concept of crucial interest to us. If we take Jürgen Habermas as the main influence with regard to the idea of deliberative democracy, we can see in his work the tendency to place the problem of autonomy in a communicative (or interactive) context: it would have to do with a relationship between autonomous *subjects*, in which the condition of being a subject, and so of being autonomous, is preserved in the case of each of the participants, by contrast to the instrumental (or work) context, which involves a relationship between subjects and objects. Of course, there is also the possibility of speaking of *strategic* interaction, where other people (other subjects) are frequently dealt with as objects, even though effectiveness in dealing with them may require that their capacity as subjects be taken into account.

In any case, some difficult questions emerge right away if we start from the contrast between instrumentality and communication. To begin with, it is hard to keep the two contexts analytically apart from each other. Even Habermas' "ideal speech situation" (where any element of power is supposed to have been eliminated and the only thing to count is the force of the better argument) is, of course, a desideratum to be *instrumentally* achieved (if at all), and communicative *action* is also action, which means that it inevitably involves itself a problem of efficacy: we have norms and sanctions aimed at ensuring the autonomy of all, and the ideal speech situation supposedly creates, in Habermas' own words, *competent* communication, despite the fact that the attribute of being competent or incompetent is in principle, for

Habermas, something that characterizes the observance of technical rules (in work) or of valid strategies, that is, the sphere of instrumentality.[1]

Moreover, it seems impossible to keep the value of autonomy, as such, apart from the strategic level, or the level of "self-affirmation" (to take Habermas' definition of *interests*, which was previously formulated in a similar way by Alessandro Pizzorno in terms of "distinguishing oneself").[2] There are two apparently contrasting meanings associated with "autonomy". The first is autonomy as self-affirmation: we deal here with an actor who is capable of just following her impulses (or spontaneously affirming herself), and autonomy in this sense is akin to the idea of power as something that allows the actor not to have to learn.[3] The other is autonomy as self-*control*, involving the idea of impulsiveness being restrained by a compulsion that is to some degree chosen and therefore the result of a reflective posture (or by *norms* that are chosen and so of one's own responsibility, in accordance with the etymology of the word "autonomy").

Now, despite the apparent contrast between the two meanings, some interesting insights may be gained if we relate the ambiguity they bring about to the difficulties faced by Habermas himself in his attempt to distinguish between "public" autonomy and "private" autonomy in *Between Facts and Norms*.[4] Even though the idea of republican virtue (with its affinity to communicative deliberation not contaminated by strategy, interests and power) favors the idea of autonomy as self-control, which suggests the restraint on my impulsiveness produced by paying attention to the connection between my self-interests and the interests or goals of the collectivity, will it actually be possible meaningfully to speak of autonomy without reference to any component of self-affirmation? Habermas sustains that the realization of supposedly "political" or "public" autonomy involves the affirmation of citizens in the political sphere, in the capacity of authors of the law (which would be a necessary condition for private autonomy to exist at all); can this be seen as involving autonomy in a way that actually eschews the component of self-affirmation, regardless of the fact that this "self" may refer to an identity or an ideal of life that turns out to be largely conditioned by the immersion in the collectivity? Even if we stress the connection between autonomy and reflectiveness, the "noble" idea itself of autonomy as self-control can be shown to assume (as is very clearly the case in the theory of moral development elaborated by Habermas himself, on the basis of the work of Lawrence Kohlberg and Jean Piaget)[5] the ability on the part of individuals to "decenter" and detach from society and its conventional norms in "post-conventional" morality. It thus supposes choice with regard to one's very identity – with inevitable ambiguity as to the relationship between the aspect of self-affirmation and the component of selflessness that the idea of self-control also evidently contains. Can the distinction between private autonomy and public or political autonomy be effectively sustained in the context of such questions?

This suggestion (the connection between autonomy, on the one hand, and reflectiveness and detachment with regard to society, on the other) can itself be linked to the problems dealt with in the literature of which Timur Kuran's book on *Private Truths, Public Lies* is an important recent example.[6] Kuran's central concern is the oppressive character that "public opinion" may acquire, with the pressures exerted by it upon individuals leading to the falsification of "private opinion". The conditions in which this can be seen to occur range from the phenomenon of "pluralistic ignorance" produced by authoritarian censorship and repression in the countries of "real socialism" or other political dictatorships (making it impossible for people to have an accurate evaluation of the degree of support with which the regime actually counts among the population) to the opinions deemed to be "politically correct" in democratic countries, private adherence to which, as shown by survey researches, is often much less widespread than one would think by looking at their public effects. Of course, the phenomena pointed at in Kuran's work and its antecedents are in clear contrast to an idealized conception of the "public sphere" as being characterized, to any important degree, by political judgments supposedly resulting from authentic *arguments*. And the outcome is that, from the point of view of the democratic ideal and of autonomy as a value, what we have to face in the relationship between public opinion and private opinion is, again, at least ambiguous: if, on the one hand, the old findings and suggestions on pluralistic ignorance, as well as their recent use by Kuran and others, point to the libertarian potential of the unimpeded flux of communication among citizens, on the other hand we are reminded by observations such as those on the "politically correct" of the themes of the "psychology of crowds", and of the sense in which, for instance, the secret vote (by *protecting* private opinion, one might say, from public opinion) is a democratic achievement.

If we think of the notion of citizenship, these ambiguities with regard to the idea of autonomy (public or political versus private autonomy, the potential benefits of communication for autonomy versus the undesirable pressures of public opinion) assume a neat character in connection with the different meanings of "citizenship" in the context of the liberal and republican traditions, which were the object of Benjamin Constant's classic essay on the liberty of the ancients and of the moderns. Years ago, George A. Kelly transposed these different meanings in terms of a distinction between the "civil" and "civic" concepts or dimensions of citizenship.[7] The "civil" dimension of citizenship (liberal and "privatist" in inspiration) is the one to stress the modern value of autonomy of the citizen before the other citizens and before the state. The real citizen, in this perspective, is that capable of affirming herself by her own means, who claims her *rights* or seeks to promote whatever interests she has, being able to mobilize in an independent way resources that are controlled by her in the private sphere or in the market. By contrast, the "civic" dimension of citizenship refers to the value of the civic virtue supposed to characterize the classic

Greek polis and the Roman republic. Instead of the idea of rights, the idea of solidarity and of the *duties* of the citizen would prevail in this case, and the real citizen would rather be the one who acts in accordance with his (the masculine gender is imperative if we deal with classic citizenship…) responsibilities before the collectivity, if necessary with personal sacrifices – even, in the limit, the sacrifice of life itself.

Current discussions on citizenship and related subjects have been strongly marked by the ambivalence and tension produced by the simultaneous adherence to the values corresponding to each of the two dimensions, civil and civic, liberal and republican. We have, on the "civil" side, the value involved in the idea of citizenship as autonomy and self-affirmation, which contains, however, the counterpart of its affinity to egoism and "privatism". On the other side, we have the value corresponding to the cohesive and altruistic substratum of citizenship as civic virtue. If, even in the classic polis, the safety of each depended on the collectivity's being capable of acting in a united or joint way, today this value has an important concrete expression in the welfare state or, more generally, in the *social* content that citizenship came to acquire and that T. H. Marshall linked to achieving the status of full and equal member of the national community, instead of the give and take proper to the market. But the value of solidarity has, in turn, the counterpart of individual dependence, which, in the welfare state, appears in the protection given by the state, in its capacity as the agent of the community, to those who are somehow incapable of fully and independently affirming themselves. More or less recent analyses of the theme of citizenship, especially in the literature concerned with social policies by the state, tend to move, often in a confusing and incoherent way, within the space distinguished by the tension between the two values.[8]

II

Now, stressing the relevance of strategic aspects is not tantamount to denying, in an abstract doctrinaire level, the crucial importance of communication and debate as an ultimate reference of the democratic ideal and its emphasis on autonomy. Actually, the idea of a process of collective deliberation guided by the search for unanimous agreement is inevitably present, I think, as an underlying utopian assumption of the very idea of politics. In this perspective, defining the object itself of political science necessarily involves a critical posture, and the conventional and trivially "realistic" reference to power relationships as the defining element of politics in handbooks of political science can only be seen as adequate if it is understood as involving the assumption that power is a *problem* to be dealt with at the practical level: we would have no politics in a society of slaves where the latter had no chance whatsoever of ceasing to be slaves and affirming themselves autonomously. In other words, there are good reasons to recover Hannah Arendt's Aristotelian insight, based

on an idealized view of the classic agora, of politics as a process of communication among equals which *excludes* power (to which Habermas is indebted, as recognized by him).[9] Of course, the big issue is how to reconcile this attractive insight with the diffuse presence of the strategic ingredients stressed by the "realistic" conception of politics – or, more abstractly, how appropriately to grasp the ubiquitous play involved in such dichotomies as friend and foe, speech and communication in contrast to potential or actual violence, solidarity and convergence in contrast to interests and conflict, autonomy in contrast to civic virtue.

In any case, if we start from the principle of unanimous agreement, strict adherence to it is clearly impossible in most circumstances of daily socio-political life. But collective debate or deliberation can be shown to underlie as an assumption the two most important procedures through which realistic accommodations of the utopian ideal of unanimous agreement are sought. The first is majority rule, which is clearly based on viewing unanimity as something capable of occurring in different degrees: the more votes in a certain direction, the "more unanimous" the decision (otherwise, there would be no reason to give precedence to the preferences of the majority over those of the minority and to adopt the former as the preferences of the whole collectivity). The other one, akin to old conceptions regarding the philosopher-king, has to do with assumptions as to where (or whom) better arguments would come from: since it is impossible actually to discuss and deliberate in an appropriately lengthy way, let us delegate the decisions to people of greater knowledge in the relevant fields (the physician, the judge and so on, or perhaps just people that we choose as our representatives and leaders and to whom we give the conditions needed for them to devote themselves to the issues to be decided upon).

It is useful to stress the affinity of this perspective to Robert Dahl's examination, many years ago, of the criteria that should guide the democratic organization of a society.[10] In Dahl's view, they are the criteria of personal choice, economy and competence, which I interpret here in a somewhat free way.

The criterion of personal choice clearly refers to the idea of autonomy as a central value. In principle, those decisions in which I am concerned are to be made by myself. Since, however, the same principle applies to all, in collective decisions (that is, in situations in which debate should ideally take place) the practical translation of the principle leads to the idea of political equality and to the search for rules akin to it: unanimity and veto rights, if possible, or, more realistically, majority rule. Let us note here, however, that there is an important alternative in which the criterion is satisfied *outside* the sphere of debate and dispensing with debate. I refer to the *market*, or to market-like mechanisms, in the operation of which, instead of deliberating together, debating and perhaps voting, people just *act* on their own and *do* as they please, with spontaneous adjustments to each other's behavior (in the formula adopted by Adam Przeworski to define the concept of "equilibrium" in a paper of a

few years ago, "everyone does what is best for himself or herself given what the others do").[11] Of course, market mechanisms involve risks of *denial* of the possibility of personal choice: not only is everyone exposed to the inconveniences or (in the language of economists) "externalities" stemming from the free behavior of others and its consequences at the aggregate level, but also "what the others do" may result in introducing elements of power and inequality, with monopolies and oligopolies. But, if the market presents such "external" costs, organizing and having people participate in collective decision-making has its own ("internal") costs, which lead to the need to resort to another of the three criteria, the one of economy.

The criterion of economy emphasizes precisely the costs involved in collective decisions and seeks to reduce them. In contrast to the frequent adherence without qualifications to participation as a desideratum (which tends to forget the *value* of being able just to go home and be left alone...), a society that required full-time devotion to collective deliberations would be clearly problematical, and the question then becomes the one of establishing which degree of public involvement would be adequate to ensure that the interests or basic values of each (that is, autonomy) be preserved. Obviously, it is the criterion of economy that points to the problems related to the need for realistic accommodation of the utopian model of deliberation in different cases. It is clearly involved in majority voting as a compromise both with regard to unanimity and, in the case of the electoral choice of leaders, in the realistic acceptance of *representation*, instead of forms of direct deliberation by all that an ambitious conception of the deliberative ideal tends to envisage. But delegation based on competence, the remaining criterion discussed by Dahl, can also be viewed as justified, in the last analysis, by considerations of costs.

The criterion of competence has to do with the supposedly superior qualification of some people or their greater control of relevant information as a reason for delegating decisions to them, in line with the philosopher- king perspective mentioned above. Its connection to the idea of costs is clear enough, since nobody can be expected to be able to invest at any given moment the amount of energy and resources needed for arriving by herself at good decisions on the problems that emerge. But, though this is not stressed by Dahl himself, reference to the criterion of competence introduces in a particularly clear way a problem that is present whenever we have representation and decision by some people on behalf of others. Of course, the mere fact that someone else is better informed on a certain subject would hardly be a reason for me to accept her decision on my behalf if I could not assume that she *identifies* with me and does indeed have my best interests in mind – otherwise, her greater knowledge or information may actually be something to be *feared* by me.

An important aspect of the problems that hinge upon this has to do with the theme of technocracy (a salient concern, of course, of the tradition of thought, including the so- called Frankfurt School, to which many of Habermas' ideas are

related). A crucial characteristic of a technocratic perspective may be pointed out in the tendency to assume that the ends are given and non-problematic, whence it would follow that the relevant issue is the degree of "technical" knowledge or information concerning the means to achieve the ends. On the contrary, democracy is based on the assumption that the ends *are* problematic: relevant ends are numerous, pertaining to different and occasionally antagonistic collectivities of various sorts and to the many individuals, and the decisive challenge is then the one of how to reconcile and accommodate these multiple ends. Of course, with regard to the definition of ends themselves it could hardly be sustained that experts or specialists should be given precedence over ordinary citizens. This has important implications for the role of cognitive resources in connection to the general theme of democracy, participation and deliberation: whatever the realistic reservations to be introduced as to more radical or ambitious formulations of the deliberative ideal, there inevitably remains, to some extent, the need for mechanisms that may allow ordinary people to be able at least to inquire about and obtain an appropriate grasp of the way in which different policies as "means" (perhaps at different levels of more or less complex chains of ends and means) articulate themselves with the "ultimate" ends to be pursued – if need be by properly interrogating the experts.

But, even if we put aside the specific issue of technocracy, the general problem posed by representation maintains itself. Either we must assume an extraordinary degree of identification between representatives and represented or some form of control of the former by the latter will be necessary. Access to different degrees of information combined with the lack of complete identification and trust in the relationships between representatives and represented is, of course, the central point of the so-called principal-agent theory, elaborated in such new fields as Joseph Stiglitz's "information economics" (or, in general, in what some have called "post-Walrasian economics").[12] Problems relating to this are clearly important in the life of economic corporations, as is the case, for instance, in the relationships between owners and managers. But they are also crucial, of course, in the political sphere, above all with regard to the relationships between citizens as principals and elected officials as agents: which mechanisms will be necessary to assure responsiveness and accountability on the part of the latter?[13]

III

Whatever the difficulties in trying to translate into practice the ideal of free and "authentic" debate, we already have at play, in the institutional apparatus of democratic states, many arrangements in which the deliberative ideal is approached in some degree and mechanisms suggested by criteria like Dahl's ones are combined in different ways. Thus, we have the legislative arena (parliament or congress), marked

by an explicit deliberative intent, though based on the representation of interests and collective identities by means of elections and often resorting to majority rule; the judicial sphere, with frequent recourse to the presumption of special competence in the figure of the magistrate, but also with the popular jury in which representation of opinions and identities is somehow introduced, despite the role of open contest and debate; spaces (councils in several niches of the state apparatus, or in institutions like the universities) where deliberation often gets actually close to a consensual or unanimity principle; and so on.

In connection with this variegated institutional experimentation, some problems of special interest emerge with regard to both the tensions and peculiar linkages between the search for authentic debate, on the one hand, and the "realistic" representation of interests and identities, on the other.

To begin with, there are the problems raised by "legal realism", discussed by Ronald Dworkin in *Taking Rights Seriously* and emphasized by Francis Sejersted, some years ago, in a discussion of the transition from liberal constitutionalism to corporate pluralism in the case of Norway.[14] The basic point is that we may have better conditions for effective democratic deliberation and collective decision-making (that is, for debate in which different points of view are effectively taken into account) if we give proper representation to the interests affected by the decisions, that is, if we *democratize* deliberation. Of course, this point is trivial in a certain light, for it lies behind the very idea of representation in general. But, as pointed out by Sejersted, "this principle is in conflict with the liberal notion of the impartial judge saying that those who have particular interests in a case should be regarded as disqualified to decide in this case".[15] And it must be added that it is also in conflict with the idealized view of debate based on the mere force of arguments, for to assume the need for actual presence of representatives of the different interests in the process of deliberation is to admit that this process will inevitably be marked by *strategic* interaction, or by factors that should be seen as spurious from that idealized point of view: even arguments or the reference to supposedly impartial rules may turn out to be rationalizations in the negative sense of the word. Looked at in the perspective of discussions dealing with "proceduralization" understood as a way to make actual processes of collective deliberation to get closer to the model of authentic debate based exclusively on arguments, this seems clearly contradictory, for restricting the role of "competence" and amplifying the space of open strategic interaction among interests appear as a way to *improve* the results of deliberation processes with regard to something that should be central to that model, that is, the ability actually to consider different viewpoints.

As indicated by the context of Sejersted's discussion, an important ramification of such problems is the question of corporatism or "corporate pluralism" (as some, including Dahl and Sejersted himself, have called it, with certain ambiguous overtones).[16] Corporatism involves deliberations in institutional spaces that bypass the

traditional mechanisms of electoral and parliamentary representation. In this regard, the resistance opposed to corporatism in the name of democracy is well-known, for mechanisms of corporatist deliberation also frequently involve some degree of informality, lesser visibility and the creation of monopolies of representation, besides supposing a rather important ("authoritarian"?) role by the state as the promoter of corporatist encounters. However, corporatism and its supposedly negative traits of this sort (though disguised under such labels as "corporate pluralism" or "*neo*corporatism") have evolved, in countries with a long liberal-democratic tradition, from the socio-political dynamics of a previous and authentically liberal and *pluralist* structure itself – which occurs largely as a mere response to the strong incentive for interests with less "natural" access to the state, for being to start with less provided with power resources of various sorts, to organize themselves so as to compensate this deficiency. Moreover, the feature of democratization stressed by Sejersted with regard to this process is undeniable, as corporatism makes possible for a category of agents (the workers) previously less present in socio-economic decisions of crucial interest to them to increase their participation in such decisions beyond the indirect influence that can be exercised through electoral mechanisms, by getting functional representation *as workers* in corporatist circles. This has been seen by some authors, with good reasons, as a decisive development even from a point of view prone to emphasize the importance of electoral democracy, for it would be a crucial part of the "social compromise" that has underlain democratic stability after the Second World War, particularly in the countries openly adhering to social-democratic arrangements. In this perspective, corporatism associates itself with the welfare state and the Marshallian social enrichment of the very idea of citizenship (besides its civil and political dimensions). And the new developments taking place with intensified globalization, by sending again to the rough sphere of the market the elements pertaining to the social dimension of citizenship and compromising corporatist structures, can also be seen as jeopardizing democracy itself.[17]

Furthermore, embroiled in all this there are also the complicated problems of *identity*. To start with, these problems underlie, of course, the above-mentioned question of the extent to which we have identification and trust between representatives and represented. But questions of identity apply in a peculiar way to majority rule itself, which involves, as part of the assumption of "degrees of unanimity", the one that agents or voters are interchangeable and their wills or manifestations of preference can be aggregated. This amounts to treating identities, in any more or less ambitious sense of the word and particularly in their connections to collective categories of different sorts, as irrelevant: people (voters) have only somewhat myopic interests or preferences ("given" or "exogenous" preferences), or, at least, they are assumed to be similar enough with regard to fundamental factors of identity so as to allow that issues of *intensity* of preference or of preference formation and

transformation (which do involve identity and may add up, for instance, to character-planning) be put aside. This is made especially clear by the contrast, to which Arend Lijphart in particular has given attention, between majoritarian systems and "consociational" or "consensual" systems: the latter emphasize precisely the need to give proper representation to shared identities whose importance for the people involved (having to do with territorial identities leading to federalism, ethnic or religious identities, and so on) should forbid that they be dealt with in terms of merely counting heads, with the possible consequence that collective identities of deep significance be permanently placed in a minority position and their interests of whatever nature disregarded.[18]

I would like to add a few observations to this. The first is that problems analogous to those of consociational representation are involved in the theme of corporatism. In other words, corporatism has to do not only with "interests" in a restricted sense, but also with identities: it has to do with the representation of a certain *category* of people which, though referring to occupational criteria, may acquire a significance for the definition of individual identities that turns out to be analogous to the one we have with ethnic or religious groups. Actually, a decisive part of the process leading to social-democracy, as well as of its importance for the stabilization of democracy as such, is linked to the fact that the inclusion of workers' organizations in corporatist deliberations helped to neutralize or reduce the political importance of the relevant identities and, by the same token, to reduce the importance of the risk (or the perception of risk) of anti-capitalist revolution in the day to day politics of the countries involved.

The second observation concerns the fact that the latter aspect (reducing the political importance or saliency of collective identities) corresponds to a trait of a *general* nature at play in the process of establishing and consolidating democracy, of which the social-democratic experiment in its various forms was one case, now possibly at risk. The relevance of stressing this is to point to another facet of the seeming paradox mentioned above: representing interests, that is, creating an arena for the strategic play of interests to assume an institutional character, though apparently in conflict with the idealized model of debate, turns out to be a decisive way to create a set of conditions that favor the actual operation, in various settings, of processes of collective deliberation, instead of the threat or actuality of open conflict. This has been dealt with in the literature, for instance, under the label of "segmentation", with which the tendency for problems of identity to unfold into belligerent dispositions may be neutralized and the political process may come to assume a "de-ideologized" nature eventually marked by tolerance and the willingness to negotiate or debate.[19] But let us note something else: if this set of conditions favors the creation of spaces of discussion and deliberation, it also favors the general operation of the second type of mechanisms that have been related above to Dahl's

criterion of personal choice and to autonomy, that is, *market* mechanisms oriented by the "cool" and perhaps "rational" search for one's interests.

IV

Let us look for a moment at the state as such in connection to the general problem of the difficulties in the relationships between the "realistic" consideration of interests and (occasionally antagonistic) identities, on the one hand, and the proper attention to aspects leading to convergence and solidarity that are assumed by the ideal model of deliberation, on the other. The central issue here has long been whether the state should be seen as the chief instrument of convergence or solidarity (of *production* of collective power, or power over "nature", to be exercised in the interest of all) or as the strategic instrument of domination of some people over others (or as part of the problem of the *distribution* of power among citizens). Some relevant observations can be made if we consider the issues by reference to the many (and confused) discussions – within or outside Marxist circles – on the so-called "autonomy of the political" (often taken to mean autonomy of the state itself).

There are a few clearly different ways in which the formula of the "autonomy of the political" is usually understood, including an analytic or methodological one and others that might be called "substantive" or theoretical. If we take the formula in methodological terms, in which it refers to a problem of *causal* relationships between different spheres in competing analytic models, there seems to be no way to avoid resorting to an old postulate in the social sciences which gives a "sociological" answer to the basic query involved: the characteristics assumed by the state are seen as dependent on a substratum corresponding to the *social* distribution of power. In this perspective, the fact that the state turns out to be, to some significant extent, either the expression of the will of all (the public interest) or rather a tool appropriated by some and used in the last analysis to repress and exploit the others depends, in principle, on the form of the play of interests that takes place at the level of society itself and on who prevails in it (Marxists would say it depends on the class struggle). All the postulate amounts to is looking at the state as part, after all, of society, and it is not at all incompatible with recognizing the occurrence, occasionally, of a large degree of "initiative" on the part of the state. But two things of interest to us can be said if we start from this analytic or methodological postulate.

Firstly, adhering to it does not amount to giving any determinate answer to the questions involved in the various "substantive" meanings attributed to the formula of the "autonomy of the political". Three such substantive meanings can be distinguished: the one of the extent to which the state is socially "neutral", or neutral with regard to class interests; the one of the "presence" of the state or of its just-mentioned capacity of initiative ("stateness"); and the one of the extent to which the

political arena has been properly institutionalized and thus protected from the changing results of the day to day vicissitudes of the sociopolitical process (the "autonomy of the political arena", as Huntington's old phrase has it, in contrast to the "praetorian" condition where institutions are weak and social conflicts express themselves through the use of whatever means, including violent ones, directly in the political arena).[20] Secondly, and more important to us: the crucial – both theoretical and practical – problem from the political point of view, the one of establishing and consolidating democracy (which is clearly related to the latter Huntingtonian perspective) reveals itself as something that turns around a certain *articulation* of precisely those three substantive meanings of the "autonomy of the political", in the framework provided by the methodological postulate. For just as we can have a state which actively *intervenes* because it is *not* neutral, or because some of the actors involved in social conflict have been able to control it once and for all (consider the idea of "dictatorship of the proletariat", or the experience of the authoritarian Brazilian regime of 1964, where we had the combination of strong interventionism with an obvious bias as to the social links and loyalties of those in charge of the state), so we can also have stable and consolidated (institutionalized) rules of the game, even formally democratic, which nonetheless turn out to consecrate open or veiled relationships of domination (consider the idea of "structural dependence" of the state on the interests of capitalists as something inherent to capitalism, or the diagnosis of the "technostructure" made by John Kenneth Galbraith many years ago with regard to the United States).

The upshot is that, insofar as the state is concerned, the problem of democracy, in an ambitious sense of the word, is precisely the one of creating the conditions (which are by force largely social, though inevitably including the challenge of "artificial" institution-building) for the state to *be* neutral: how to establish a "social compromise" that may allow the state itself an important degree of *autonomy* in the face of strategic relationships and likely asymmetries in the dynamics of private interests, so that it becomes possible for the state to *intervene* not only to guarantee the "liberal rights", but also to try and *compensate* for inequalities in the social distribution of power and to ensure the "positive liberties" in which everyone may come to have better conditions of self-realization.

Now, this conception of an autonomous state is clearly in conflict, in a way, with the ideal of "popular sovereignty". The latter supposes a homogeneous public to which the state should be subjected, whereas the above suggestions refer to unequal societies and to the risk that subjecting the state to society may result in its subjection to the powerful citizens and in making it into the famous "committee" for the promotion of their interests. But there is another point to be stressed in connection to our main concerns here. It has to do with the fact that, in spite of all the previous emphasis on the need properly to represent interests in the state,

there is no way to avoid recognizing that the state we want must be, to a large extent, a *paternalistic* state – that is, a state that is not restricted to reacting to the differential ability to exercise pressure on the part of the various private foci of interests or identities. The recognition of this requisite is reinforced by the impossibility of representing *all* interests, which in many cases never reach the stage of becoming vocal and affirmative. Let us put aside the question of the degree to which a properly "virtuous" disposition would have to be enshrined in such a paternalistic state, or else if we could count upon efforts at realistic institution-building of the kind seen as characterizing the ideas of the "Founding Fathers" of the United States, in which the public interest is somehow safeguarded through the institutional play of egoisms or "factions": the main thrust of our argument certainly recommends the latter, but there seems to be no escape from some degree of appropriate cultural or sociopsychological conditions in operation in the society at large. But one further point can be made, as a relevant ramification of the previous observations. To wit, the old problem of the tense relationships between capitalism and democracy, usually taken in terms of *political* democracy, actually occurs in a crucial way in connection with the question of *social* democracy: not only the possibility of "revolution" – or of the rupture, however it may take place, of prevailing socio-economic power relationships – is perhaps the decisive factor in conditioning democratic instability, but also the operation of an effective democracy cannot avoid somehow facing up to the aim of social democracy.

V

Before closing these notes, let me go back to the idea of the operation of market mechanisms and explore some ramifications of it. Despite both the negative and positive mythologies that surround the notion of market in age-old political confrontations, I think it can provide the focal point for a sort of "realistic utopia" capable of reconciling the tension between the two dimensions of, say, "solidarity" and "interests" stressed above in various ways. If we consider again the idea of autonomy as a crucial democratic value, there is no doubt that, whenever we are concerned with actually joint or collective decisions, this value leads to debate and deliberation and, if possible, to unanimous agreement.

But there is another aspect, besides the one of costs and practical difficulties, to the objections that can be raised to viewing deliberation, whatever its doctrinaire importance in the last analysis, as a proper foundation for a viable conception of politics and democracy. Many years ago, the economist Abba Lerner wrote that "an economic transaction is a solved political problem".[21] Now, resorting to collective deliberation cannot avoid the assumption that fundamental difficulties at the level of conflicts of interests have been solved, or that some form of "constitutional"

accommodation in the coexistence of relevant interests has been achieved (it would be possible to say, certainly with better reasons than in the case of economic transactions, that "a parliament is a solved political problem"). Note that Habermas himself, dealing in *Between Facts and Norms* with the cultural pluralism of the informal public sphere (in which the sphere of formal deliberation of a parliamentary kind nourishes itself), emphasizes the fact that it depends on "the support of a societal basis in which equal rights of citizenship have become socially effective", which points not only to "political" (or "formal") democracy, but also to "social" democracy: "Only in an egalitarian public of citizens that has emerged from the confines of class and thrown off the millennia-old shackles of social stratification and exploitation can the potential of an unleashed cultural pluralism fully develop".[22]

In any case, it seems inevitable to admit that, in the conditions proper to large and complex societies, the form *par excellence* to ensure autonomy at manageable "internal" or organizational costs involves *reducing the space in which collective deliberation is necessary* and trying to create the conditions for people to act on their own with minimal "external" costs as well. The indispensable efforts at institution-building and "proceduralization" will then be guided, at the most encompassing level, by the idea that decisions will be made, to the largest possible extent, by the dispersed actors themselves (which does not preclude resorting to procedures more akin to the deliberative model wherever feasible), and the balance with regard to the concern with both "internal" and "external" costs will be sought by reference to principles akin to the principle of "subsidiaryness" that tends to be invoked in discussions on federalism, which supposes that decisions are to be transferred to a "higher" level (from the level of individuals to that of increasingly large and encompassing collectivities) only as the nature of problems requires it.

This perspective, that some might wish to see as just "liberal" in the European sense of the word, could invoke in its support even the anarchist model of the communist society depicted by Marx in *The German Ideology*, where individualism and individual autonomy are taken to the point of capricious behavior – despite the obvious lack of sensitivity Marx displays, in this regard, toward the problem of "externalities", whence his bet on suppressing the state. But taking the notion of market as a crucial reference for the attempt at synthesis suggested here finds perhaps its clearest classic support in Max Weber's work. As Weber's analyses of the market have shown, it can be described as the locus of "sociability among strangers", in which we have the synthesis between "society" and "societal action" (distinguished by the "rational" search for interests, the "rough" side of the market that I linked above to its expansion with globalization), on the one hand, and "community" or "communal action" (distinguished by the feeling of being part of a whole), on the other.[23] The communal aspect of the market involves the operation of a principle of solidarity, however "thin", and the adherence to norms that regulate and mitigate the general-

ized pursuit of interests, thus ensuring that interest-based exchanges and interactions may recur and endure without degenerating into a Hobbesian situation of generalized fraud and, eventually, belligerence.

Moreover, by claiming the notion of market as distinguished by such traits, with the reference to the autonomy of agents (and thus to their equality, which excludes power relationships and so oligopolies and monopolies from the market in a strict sense), I can ascribe to it a scope and a relevance that go far beyond the sphere conventionally thought of as "economic", making it appropriate to speak of a sort of "political market" as a regulating idea capable of encompassing important aspects of the democratic ideal. This suggestion can best be appreciated through a reevaluation of the notion of interest itself. Current usage tends to link "interests" above all to the economic sphere defined in a rather narrow way, in connection with values or objectives of a "material" nature. But if we approach the notion of interest as generically equivalent to the idea of "self-affirmation" (or "self-distinction", to give Pizzorno his due), we can then see that it is logically intertwined with the ideas of power and of strategic interaction – and there clearly is no reason to restrict the category of the market, seen as the locus of the play of interests, to the economic arena. Actually, the reference to "interests", "strategy" and "power", as well as to the affinities among them, turns out to provide a fundamental criterion for an *analytic* definition of politics as such, by contrast to the blunt reference to the state as a sort of concrete "piece" or part of society that we often find, either explicitly or implicitly. According to this analytic definition, politics would consist of strategic interactions and the search for self-affirmation or for power in any concrete institutional or social context, independently of the specific content of goals that may be the object of conflict or cooperation in one sphere of interaction or another – that is, material or "economic" goals or goals relating to religion, class, race, ethnic groups, gender, generation, and what not. In other words, politics, understood as the interplay among interests and its eventual accommodation, has no content of its own and is socially ubiquitous: it penetrates social relationships of all kinds and pertains to the "social basis" of conflicts and to the potential or actual foci of solidarity and group identification that become engaged in such conflicts – just as it pertains also to the organizational expression of conflicts and solidarities at the level conventionally referred to as "political" or "politico-institutional", where the factor of convergence represented by an appropriately complex and effective state affirms itself, lest the play of interests should lead to Hobbes.[24] Again, as previously said, the deliberative utopia can be seen as a guiding idea, and so a relevant component of the definition of politics, involving a bet on the just-mentioned organizational (and parliamentary) expression of conflicts; but it is precisely the unquestionable centrality of strategy, interests and conflicts in politics that justifies, as we just saw, looking at deliberation as a "solved political problem".

Of course, by thus amplifying the reach of the notion of market we end up with the old idea of the pluralist and individualist society. In this society, the prevailing conception of civic virtue is a rather mild one, understood as "tolerance" – precisely the sociability or solidarity "among strangers", or the "out-group morality" dealt with by Wolfgang Schluchter,[25] which is in clear contrast to psychological fusion and effusiveness and to the risk of fanaticism and belligerent leanings that go with them. Provided with this form of civic morality, autonomous individuals are able not only to choose their associates and loyalties in different specific spheres, but also, as we noted above with regard to autonomy as self-control, their personal identity itself. So, the ability of individuals do "decenter" and detach themselves from society, besides its obvious connections to a "nobler" sort of autonomy (or to *real* autonomy) and to the possibility of neutralizing the political relevance of questions of identity and related ones, becomes the condition for a reflective sort of solidarity which stops short of the negative overtones of the sheer immersion in society and identification with it. To be sure, there is a clearly paradoxical aspect to this, from which there seems to be no escape: if we are to have the actual institutionalization or enshrinement of a democratic and pluralistic *culture* in this sense, so as to avoid the problematic condition in which individuals would be supposed judiciously to ponder their actions at every moment, it will be necessary, on the one hand, that an ethic broadly shared by the collectivity as such comes to operate routinely; but, on the other hand, this ethic – as such inevitably "conventional" – will have to be of such a nature that it stimulates individual autonomy and "post-conventional" forms of morality.

In a way akin to the idea of a market in operation, all this amounts to eliminating or minimizing the role of *ascription* and of the inequalities associated with it, even though the relevant choices are inevitably exerted over a "raw material" which is itself always *social*, or socially given or imposed: there is, of course, no point in looking "back" to a pre-social "state of nature" where one would supposedly be authentically oneself. Besides the links one might point here to a long tradition of thought in general sociological theory, there is certainly no need, with regard to the more directly political implications involved, to mention the long "pluralist" line of thought ranging, for instance, from Tocqueville through William Kornhauser to Robert Dahl. But perhaps there should be a mention to a book of a few years ago by Ernest Gellner, *Condições da Liberdade*. [26]

The reason for this mention concerns one of the negative models of society to which the positive model of the pluralist society (called the "civil" society by Gellner) is opposed. These negative models usually include two "modern" categories: the "mass" society, where atomized and socially uprooted individuals relate without social or group intermediations of any sort with the state, and the "totalitarian" society, where an invading state seeks to control all aspects of individual life and socio-political interactions.[27] But they include also the "traditional" or "communal" society.

Being present both in Kornhauser and in Gellner, this model of society is elaborated at length by Gellner, who stresses in a particularly vigorous way its negative traits. Communal society is depicted by him as "strongly making the individual a mere part of a social unit" and as imposing upon him or her a "suffocating" identity, which is in conflict with the "modern conception of liberty" that "includes the requirement that identities be chosen and not ascribed". Many of such negative and "suffocating" traits are seen by Gellner to be also present, still today, in the Islamic *Umma*, the "community based on the faith shared by all and in the implementation of its law", as well as in the peculiar "secular Umma of Marxism".[28] But it is especially interesting, from the point of view of our concerns here, the fact that Gellner, resorting to Fustel de Coulanges, does not hesitate to include under the negative characterization of the communal society the "ancient city" itself of Greece and Rome which provides the idealized reference for the celebration of civic-republican virtues – and, of course, for much of the deliberation literature. After all, as we have been recently reminded also by Ellen Meiksins Wood,[29] there were no civil rights in Athens. And Gellner's "civil society" as a positive model has to be contrasted also, which is done by him in an emphatic manner, to the civic society so dreamed of by many. Actually, Gellner is explicitly critical even of the idealized (or civic) view of "civil society" to be found in much of the recent literature on this concept, where – at odds with its classic use by Hegel, for instance, to whom civil society is the space of interests and particularisms, by contrast to the universalism of the state – it is associated with a public-oriented or "altruistic" motivation. It is quite obvious (and up to a point unquestionably "good") that, besides interest-groups proper, we can also have public-oriented groups or associations of various kinds as participants in the pluralist society. But the fact that divergent (and militant) conceptions of the public good may often get willingly involved in strictly strategic and even belligerent interactions, in contrast to the tolerance that the pragmatism of interests tends to induce, speaks in favor of Gellner's perspective. And this perspective should be kept in mind especially in face of the claim, by some of the recent champions of civil society, to the effect that, due to its "virtuous" character, the latter might be expected largely to replace and dispense with the state by becoming a sort of diffuse source of convergence and cohesion.

I'll leave Gellner at that. But I would like to close this section on market and pluralist or civil society with a little journalistic story, which seems to me to bring interesting suggestions in connection with the play between market mechanisms, on the one hand, and the conventional political and electoral arena, including the problem of regulation by the state, on the other. A few years ago, apropos of the manifestations that took place in Prague on the occasion of one of the IMF and World Bank meetings, the journal *The Economist* discussed the role of non-governmental organizations (NGOs) that have been frequently involved in such events.[30] Besides talking about the rapid globalization of NGOs and the efficacy of their action, as

well as the possible confusions occurring in their positions on such issues as the relationships between poverty and capitalist development, *The Economist* goes on to raise the problem of the democratic legitimacy of their behavior. Who elected the NGOs? Why can they feel authorized to call into question the decisions or acts of "law-abiding corporations", or to claim for the change of policies by democratically elected governments?

There is, no doubt, one point regarding which these interrogations are certainly well taken. It has to do with the extent to which, in the actions of protest by NGOs, legal norms are observed or, in the contrary, they are willing to resort to violence. It seems that this willingness does exist in the definition of some of the aims to be sought by the groups that oppose globalization.

If this crucial reservation is kept in mind, however, to ask for the democratic credentials of NGOs in electoral terms is clearly improper. It is unquestionably fitting to the dynamics of democracy that interest groups or categories, or groups that share opinions on problems of public interest, may seek autonomously to organize themselves so as to be able effectively to articulate and promote their interests and opinions. But there is more to this. There is an obvious question which is *not* raised by *The Economist*, though it should emerge rather naturally in a context where we are dealing with the vigorous transnational affirmation of market mechanisms, seen with propitious eyes by the journal: should we ask for the electoral-democratic credentials of "lawabiding" corporations, whose decisions frequently affect in so dramatic a way the lives of so many people? One might recall here Robert Dahl's perspective in a work of many years ago, where the author, calling large corporations "pseudoprivate" precisely due to the public impact of their decisions, stresses the need for democratizing such decisions through some form of representation of affected interests.[31]

If requiring electoral-democratic credentials in the case of agents of the market conventionally seen in economic terms seems absurd, despite agreement on the obvious need for state regulation, the point is to emphasize that perfectly analogous market-mechanisms do have an important place in the socio-political arena as well, though state regulation is obviously needed also here. The general problem, once more, is how to reconcile in an adequate way the public interest with the autonomy of agents in the search for their goals of whatever nature. And if safeguarding the public interest supposes regulation – of which electoral procedures can be seen as an instrument – capable of ensuring democratic values, the autonomy that expresses itself directly in the market (or in "civil society") is also a crucial democratic value. Up to what point should we regulate democratically and politically the economic sphere, and how far should we allow the autonomy of the market to penetrate the conventionally "political" sphere (no doubt including the sphere of the "civil society" in the sense of the recent literature on this concept)?

VI

In the world of globalization and of the transnational affirmation of economic and financial markets, there seems to be no doubt on the desirability not only of reinforcing, if possible, the regulatory powers of states at the national level (though we now have states and states, with very different capabilities with regard to exerting influence on national and international spaces), but also of effectively establishing the functional equivalent of the state, and so a factor of convergence and control, at the transnational or international level itself where those markets tend increasingly to operate. It is also clear that, however difficult and unlikely the fulfillment of this task may be (among other things for the asymmetries themselves between the national states and the lack of a substratum of real *community* at the planetary scale), instituting the functional equivalent of the national state at the international level would involve creating forums of debate and deliberation that might be far more effective than the ones presently available.

Perhaps less clear, however, is the need to create and expand the market itself. For, the transnational overflow of economic and financial activities notwithstanding, there is a clear sense in which markets have actually been shrinking. I refer to the Hobbesian feature of globalization, in which the harsh new competition of a globalized world is accompanied by new forms of inequality and exclusion, with the crisis of Keynesianism and social-democracy, unemployment, the diffusion of informal and precarious kinds of work relationships, increasing urban violence and, especially in the United States, "hypercriminalization" and the explosion of incarceration rates and of the correctional population.[32] Of course, in a country like Brazil, the impact of exposure to these new processes will tend to have a cumulative character, in which they combine with the huge inequality and caste-like forms of social stratification inherited from our centuries-long experience with slavery. Needless to say, for most of those submitted to the material and intellectual deprivations associated with such conditions, the prospects of autonomous participation in significant processes of collective deliberation are paltry indeed. And we should probably keep in mind the need for long-run developments in which, among other things, indispensable paternalism on the part of the state might help create the conditions for more widespread and appropriate access to the material and intellectual resources needed for the significant emergence of identities eventually capable of autonomy and political expression, instead of the increase in criminal behavior we now have as the most evident manifestation of our lasting defficiencies. In this perspective, "creating market" can be read as creating the conditions for competition to stop being, for many, a fraudulent game, or national competitiveness a synonym to social exclusion.

NOTES

***** In preparing this paper, I had to work in a rather hasty way. So, as someone has said (I don't recall who), I didn't have time to be brief, or perhaps to be as organized, tight and cogent as might be desirable. But I hope my main purpose – to confront and complement a philosophical or doctrinaire way of looking at deliberative democracy with a "sociological" and "realistic" analytic perspective – is served well enough, and that the paper in its present form may be of some help in our discussions.

1 The critique of the separation between instrumentality and communication has important ramifications with regard to the idea of rationality itself and the attempt to distinguish a so-called "merely" instrumental conception of rationality and a supposedly alternative one, presumably of a "substantive" kind, which has a point of departure in Max Weber's inconsistent distinction between means-ends rationality and value rationality – a part of the conceptual hodgepodge in which Weber seeks to establish types of rationality by reference to ethics and types of ethics by reference to rationality. The work of Jean Piaget seems to me to provide a solid basis for superseding the separation of instrumentality and communication and replacing it with an "operational" perspective in which the objective or instrumental and the social or communicational aspects of rationality are duly integrated. A discussion in which Habermas' views are examined in the light of Piaget's work can be found in Fábio W. Reis, *Política e Racionalidade*, Belo Horizonte, Editora UFMG, 2000 (parts of which are synthesized in Fábio W. Reis, "Change, Rationality and Politics", Working Paper # 10, Kellogg Institute for International Affairs, University of Notre Dame, January 1984).

2 See Jürgen Habermas, *Théorie et Pratique*, Paris, Payot, 1975, vol. II, pp. 104-105; and Alessandro Pizzorno, "Introduzione allo Studio della Partecipazione Politica", *Quaderni di Sociologia*, vol. 15, no. 3-4, July - December 1966.

3 See, for instance, Karl Deutsch, *The Nerves of Government*,...

4 Jürgen Habermas, *Between Facts and Norms: Contributions to a Discourse Theory of Law and Democracy,* Cambridge, Mass., The MIT Press, 1996.

5 See, for instance, Jürgen Habermas, "Moral Development and Ego Identity", chapter 2 of J. Habermas, *Communication and the Evolution of Society,* Boston, Beacon Press, 1979.

6 Timur Kuran, *Private Truths, Public Lies: The Social Consequences of Preference Falsification,* Cambridge, Mass., Harvard University Press, 1995.

7 George Armstrong Kelly, "Who Needs a Theory of Citizenship?", *Daedalus,* fall of 1979, pp. 37-53 (*Proceedings of the American Academy of Arts and Sciences,* vol. 108, no. 4).

8 Thus, in Kelly's article cited above, the idealized, concerned and "republican" citizen is opposed, in reference to the welfare state, to the posture of the "client", which suggests a sort of "negative citizenship", as if the very success of the welfare state resulted in introducing an element of "market" in the noble status of the citizen, thus somehow degrading the latter. A similar position also emerges in texts by Habermas, where the contrast between citizen and client is placed in correspondence with the contrast between communicatively structured spheres of life, on the one hand, and the "systemic" spheres of state and economy, on the other (see, for instance, Jürgen Habermas, "A Nova Intransparência: A Crise do Estado de Bem-Estar Social e o Esgotamento das Energias Utópicas", *Novos Estudos Cebrap,* no. 18, September 1987). Differently from this tendency to favor the republican content of citizenship, the literature dealing with Brazil turns out to be, to a large extent, just confused and inconsistent, in some cases denouncing, with remarkable insensitivity with regard to the difficulties involved, both the liberal citizenship of individualistic and egoistic practices and the "passive" form of citizenship dependent on paternalistic assistance by the state (see, for instance, Maria Victória Benevides, *A Cidadania Ativa,* São Paulo, Atica, 1991).

9 See, for instance, Habermas, *Théorie et Pratique,* vol. I, p. 105, fn. 5, and p. 34.

10 Robert Dahl, *After the Revolution: Authority in a Good Society,* New Haven, Yale University Press, 1970.

11 Adam Przeworski, "Democracy as an Equilibrium", ms., New York University, 1995.

12 See, for instance, Joseph Stiglitz, *Whither Socialism?*, Cambridge, Mass., The MIT Press, 1994, and Samuel

Bowles and Herbert Gintis, "The Revenge of Homo Economicus: Contested Exchange and the Revival of Political Economy", *Journal of Economic Perspectives*, vol. 7, no. 1, 1993.

13 See Bernard Manin, Adam Przeworski and Susan C. Stokes, "Introduction", in *Democracy, Accountability, and Representation,* ed. A. Przeworski, S. C. Stokes and B. Manin, New York, Cambridge University Press, 1999.

14 Ronald Dworkin, *Taking Rights Seriously*, Cambridge, Mass., Harvard University Press, 1977; Francis Sejersted, "From Liberal Constitutionalism to Corporate Pluralism: The Conflict over the Enabling Acts in Norway after the Second World War and the Subsequent Constitutional Development", in *Constitutionalism and Democracy* (ed. John Elster and Rune Slagstad), New York, Cambridge University Press, 1993.

15 Sejersted, "From Liberal Constitutionalism to Corporate Pluralism", p. 299.

16 Robert Dahl, *Dilemmas of Pluralist Democracy: Autonomy vs. Control,* New Haven, Yale University Press, 1982.

17 The literature stressing the links between democracy and the idea of a social compromise includes, for instance, Adam Przeworski, *Capitalism and Social Democracy,* New York, Cambridge University Press, 1985, and J.-A. Bergougnoux & Bernard Manin, *La Social-Démocratie ou le Compromis,* Paris, PUF, 1979. Both Przeworski, in the book just cited, and Dahl, in *Dilemmas of Pluralist Democracy* (see p. 80, for instance), are examples of authors who expressed concern with the risks for political democracy itself if social-democracy and "corporate pluralism" are threatened.

18 See, for example, Arend Lijphart, Patterns of Democracy, …

19 See, for instance, Giovanni Sartori, *Parties and Party Systems: A Framework for Analysis,* vol. I, New York, Cambridge University Press, 1976.

20 Samuel P. Huntington, *Political Order in Changing Societies,* New Haven, Yale University Press, 1968.

21 Abba Lerner, "The Economics and Politics of Consumer Sovereignty", *American Economic Review,* May 1972, vol. 62, no. 2 (cited according to Bowles and Gintis, "The Revenge of Homo Economicus")

22 *Between Facts and Norms*, p. 308. In this regard, it may be helpful briefly to recall some results of efforts by Bowles and Gintis to map out recent revisions in the field of economics, in which the neo-classical Walrasian perspective is increasingly confronted by a variety of "post-Walrasian" approaches that "re-politicize" the field. Bowles and Gintis set up a double-entry space on the basis of the guiding assumptions of each approach with regard to both the nature of "enforcement of claims" (whether it is "exogenous" and exercised by the state with its laws and regulations or "endogenous" and so contested and conflict-prone) and the nature of agents themselves or of their preferences and norms (whether we have methodologically individualist assumptions of "given" preferences or else the assumption that preferences can be changed, be it through open conflict or, of course, debate or collective deliberation). Though the authors do not state the problems in terms akin to the "deliberative" literature, it turns out that the cell corresponding to deliberation is, of course, the one in which we have (inevitably) *endogenous* assumptions as to the nature of agents, whose preference-formation and preference-change are seen as open and so as a necessary object of study, and *exogenous* (or state provided) enforcement of claims. Exchanges corresponding to this cell are described as "contractual", by contrast to "contested" forms of exchange to be found where both enforcement and the nature of agents are seen as endogenous. Besides Bowles and Gintis, "The Revenge of Homo Economicus", see also Samuel Bowles and Herbert Gintis, "Post-Walrasian Political Economy", in *Markets and Democracy: Participation, Accountability and Efficiency,* ed. S. Bowles, H. Gintis and B. Gustafsson, New York, Cambridge University Press, 1993.

23 See, for instance, Max Weber, *Economía y Sociedad,* México, Fondo de Cultura Económica, 1964, pp. 33-35 and 496. Again, let us note how this conception of the market is akin to some views of Habermas' on some crucial traits of the public sphere in the same passage of *Between Facts and Norms* cited above (p. 308). After stressing the communicative elements needed to master conflicts and their social requisites, Habermas points, without reference to Weber, to a sort of end-state of "solidarity among strangers – strangers who renounce violence and, in the cooperative regulation of their common life, also concede one another the right to *remain strangers".*

24 I use here formulations taken from Fábio W. Reis, "The State, the Market, and Democratic Citizenship", in *Constructing Democracy: Human Rights, Citizenship, and Society in Latin America,* ed. Elizabeth Jelin and Eric Hershberg,

Boulder, Colorado, Westview Press, 1996. Though I am not entirely happy with the English revision, which produced some relevant "substantive" distortions, this text elaborates somewhat further some of the ideas touched upon here. See also Fábio W. Reis, *Mercado e Utopia: Teoria Política e Sociedade Brasileira,* São Paulo, Edusp, 2000.

25 Wolfgang Schluchter, *The Rise of Western Rationalism: Max Weber's Development History,* Los Angeles, University of California Press, 1981.

26 Ernest Gellner, *Condições da Liberdade: A Sociedade Civil e seus Críticos,* Rio de Janeiro, Jorge Zahar Editores, 1996 (original English edition, ..., 1995?).

27 See especially William Kornhauser, *The Politics of Mass Society,* New York, The Free Press, 1959.

28 Gellner, *Condições da Liberdade,* pp. 13-16, 30, 88-92.

29 Ellen Meiksins Wood, *Democracia contra Capitalismo: A Renovação do Materialismo Histórico,* São Paulo, Boitempo Editorial, 2003 (original English edition, ..., 1995).

30 *The Economist,* ....., October 2000.

31 Dahl, *After the Revolution,* p...

32 See, for instance, Jonathan Simon, "Governing through Crime", ms., January 1997.

Fábio W. Reis

PROFESSOR OF POLITICAL SCIENCE AT
FEDERAL UNIVERSITY OF MINAS GERAIS - UFMG

JUDICIAL REVIEW OF ADMINISTRATIVE ACTION: REFLECTIONS ON BALANCING POLITICAL, MANAGERIAL AND LEGAL ACCOUNTABILITY

Jerry L. Mashaw

The Puzzle of Judicial Review of Administrative Action.

Most modern democracies have at least one thing in common: judicial review of administrative action is simultaneously ubiquitous and contestable. The ubiquity of judicial review of administrative actions has two foundations. Normatively, democratic governance presumes that officials are the servants of the people. For that normative proposition to be true of any particular society "the people" must be able to hold officials accountable for their actions. But, judicial review is not the only accountability mechanism available. Its ubiquity requires a further factual predicate - the incapacity of other accountability mechanisms to ensure that officials serve rather than rule. No functioning democracy worthy of the name has found the primary alternative accountability mechanisms, political or managerial control, adequate to the task of sustaining democratic accountability. For this reason "democracy" and the "rule of law" have become inextricably linked, with judicial review as the keystone of the legal accountability system.

Notwithstanding its centrality in modern democratic governance, judicial review of administrative action remains continuously contestable. Complaints of the incompetence, impertinence and irrelevance of judicial review are at least as common as praise of judicial review's efficacy. Responding to these pervasive critiques, the specific practices and procedures of judicial review of administrative action are subject to constant amendment, revision, and, occasionally, major reform.

The reasons for judicial review's contestability, I will argue, are the mirror image of the reasons for it's ubiquity. Judicial review of administrative action simultaneously

supports other accountability mechanisms that bolster democratic governance and undermines them. The institution of judicial review of administrative action is rife with paradox. It supports *democratic* governance by making officials accountable to *unelected* judges. It protects *individual rights* while simultaneously ensuring *state control*. It legitimizes expert administrative judgment by subjecting that judgment to review by bodies who often have limited knowledge of either the technical data upon which administrative action is premised or the concrete situations within which administration must function.

The puzzle of judicial review of administrative action, therefore, is just this: how can such a necessary feature of modern democratic governance be accommodated to the demands of both effective administration and democracy itself? My approach to this puzzle is to view judicial review of administrative action as part of a broader question of governmental design in modern democracies, that is, how to make administration simultaneously managerially effective and politically responsive. The answer, in part, has been to make administration legally accountable through judicial review. But, this is a design problem that can only be managed, not solved. For, it entails maintaining an appropriate balance among competing forms of accountability in states committed to democracy, but constrained by the demands of efficacy and by the brute facts of social, political and economic complexity.

Forms of Official Accountability.

In virtually all modern democracies administrative officials are held accountable through three different, but connected, accountability regimes - the political, the managerial, and the legal. Indeed, in some sense, the emergence of the latter two forms of accountability are responses to the inefficacy of electoral control in the modern administrative state.

Virtually all western democracies labor in the shadow of the (quasi-mystical) model of Athenian democracy.[1] This was supposedly one of the few times in recorded history that government was in Lincoln's ringing phrase "of the people, by the people, and for the people". Citizens met as a committee of the whole, official positions were allocated by vote or by lot, and officials reported back to the assembly of the citizens. Ten times a year officials charged with carrying out various administrative tasks reported on the conduct of their offices. Their reports were subject to a vote of confidence; and, if confidence was lacking, officials faced a trial by a jury of their fellow citizens. In addition, an official might be impeached by the assembly at any time.

Officialdom was hazardous in Athens, precisely because electoral accountability was efficacious. Any unsuccessful battle or unproductive foreign negotiation might subject the hapless general or ambassador to trial, and, if convicted, to death or

exile. According to Demosthenes, Athenian generals were tried for their lives two or three times in an average career, and the danger of death by trial was greater than the risk of dying in battle.

That this direct and immediate approach to holding officials politically accountable no longer describes modern governance is obvious. What is perhaps less obvious is that the conditions of modern complex societies make most versions of political control of official action incompetent.

This is not to say that periodic elections under conditions of open access to office and majority rule, and the political accountability of administrators to duly elected public officials, are unimportant details of modern democratic governance. They are crucial to the political definition of democratic citizenship. They maintain a limited capacity to hold officials accountable for results based on the presumed political preferences of the electorate.

The problem, of course, is that the electorate is no longer reasonably homogenous, and the relationship between citizens' votes and the output of legislative processes is notoriously weak.[2] Moreover, for electoral accountability to function effectively presumes that elected officials can control administrative officials. In modern welfare and regulatory states the linkage between elected officials and administrators is not a myth, but it is tenuous. Administrators often possess wide discretion and the quality of their performance is difficult for elected officials to evaluate.

Wide discretion and loose oversight are not difficult to explain. The heterogeneous preferences of a diverse electorate and the uncertainties of appropriate action in a complex world are reflected in the vagueness of the mandates that legislators can provide for administrators.[3] Vagueness begets discretion. And when evaluating performance social outcomes are often complexly and only indirectly related to administrative behavior. To make matters worse much administrative action is non-observable by elected officials who can at best exercise episodic oversight over some administrative decisions. And, administrators have quasi-monopolies on the information necessary to evaluate the effects of their actions.[4] In the modern administrative state the belief that the citizen-elector exercises democratic control over administrative behavior, even mediately through elected officials, is stretched very thin.

One solution to the deficiencies of political accountability is an attempt to assert managerial control. We live in what has been called an "audit society".[5] And the "audit", broadly understood, is the managerial accountability mechanism of choice in both public and private organizations for ensuring that those who "have the doing in charge", act both competently and honestly.

Managerialism as a mode of accountability is, of course, not unique to democracies. The monarchical model of accountability involved a simple hierarchical relationship. Officials were accountable to the monarch and the monarch to God. We know little about how God kept his accounts, but monarchs rapidly developed

rudimentary systems of auditing.[6] Modern governments are rife with inspectorates of one or another type. In some cases the inspectorate is designed to reinforce political control by providing the expertise and continuous observation that politicians lack. In other cases the inspectorate is inside the bureaucracy itself. Indeed, modern managerial techniques emphasize the role of *external* audits in the creation of *internal* accountability systems that will produce appropriate controls over official (or private) behavior.

This technocratic regime reinforces accountability, but at a cost. First, it must focus on efficiency and effectiveness and on processes or systems. These are important matters, but they are complexly and sometimes mysteriously related to bureaucratic outputs or social outcomes. More importantly, they have virtually nothing to say about policy choice. They, therefore, strengthen elected officials' capacity to guard against corruption and inefficiency, but do little to strengthen political control over what modern bureaucracies do. Put slightly differently, managerial controls tend to assume that administrative implementation can be measured against clear, predetermined policy goals and that processes are tightly linked to outcome. Neither of these assumptions is realistic.[7]

Second, the language and dialogue of administrative oversight is internal to the administrative system. The expertise of administrators not only defeats direct political supervision, it defines the terms of evaluation from a managerialist perspective. Managerialism has its virtues, but strong reinforcement of democratic accountability is not one of them.

Moreover, there is the continuing problem of who audits the auditors. Here, somewhat ironically is an entryway for judicial review of administrative action. Although we moderns mostly think of judicial review as a means of protecting individual rights against administrative tyranny, judicial review has historically played another role as well. Hauling the king's officers before the king's courts to answer for their conduct promotes central administrative control by the sovereign at the same time that it protects private rights. Judicial review consolidates state power, and with the shift of power to the people in constitutional democracy, judicial review becomes a device for reinforcing the democratic accountability of administrative officials.[8]

Viewed from this perspective, judicial review of administrative action - the demand for "legal" accountability of officials - is the carrying out of a democratic political project: the reinforcement of democratic control of official behavior. But, like managerial accountability regimes, it is not obvious that the techniques of accountability available through judicial review are a good fit with the project of democratic political control. Accountability through judicial review is accountability to law. And so it must be. For, to premise accountability in courts on anything other than the law would be to undermine the democratic political accountability that judicial

review is struggling to reinforce. Judicial review can, therefore, only obliquely reinforce political accountability. And, as we shall see, translation of the political or the managerial into the legal can undermine those sources of accountability as well.

We find ourselves in the modern era, therefore, with a mixed set of accountability regimes: political accountability through electoral processes; managerial accountability through processes of audit and systems design; and legal accountability through judicial review. The project for institutional designers is to make these differing accountability regimes work together to produce accountable governance. And it is in this attempt that we uncover some of the paradoxes and puzzles of judicial review.

For, alas, we do not live in a world in which we can happily assign issues to boxes labeled Apolitical", "managerial", or "legal". Much administrative action can be characterized in all three ways, that is, it makes policy, it is based in part on administrative considerations of efficacy, and it affects citizens' interests in ways that raise potential legal issues. Much of the doctrine and argument in any legal system utilizing judicial review of administrative action is precisely about the separation of the "legal" from the "political" or "managerial". Or, perhaps better put, it is about the accommodation of these three separate means of providing official accountability. For it is the job of judicial review both to support political and administrative accountability and to assure accountability to law. The stresses involved in balancing accountability regimes show up anywhere and everywhere in administrative law doctrine.

Legal Accountability in Action

One way to see this delicate balancing act in action is to look at three paradigmatic types of administrative action that might be subjected to judicial review for legality: administrative adjudications, administrative rulemaking (or the adoption of what is sometimes called "delegated legislation"), and "informal" administrative action that neither decides a case nor promulgates a general norm. In a simpler world one might confidently assert that reviewing administrative adjudication was the principal function for judicial review. As in reviewing the decisions of lower courts, the question for judicial resolution would be straightforward, that is, "was this case decided according to law?". Rulemaking or delegated legislation would, by contrast, be just that: policy choice subject only to available regimes of political accountability (and, perhaps, judicial review for constitutionality). And informal managerial action by administrators would be subject to whatever processes of audit and accountability the relevant bureaucracy and its political overseers had devised. To some substantial degree this simple picture describes the presuppositions of judicial review of administrative action. But using some American examples, let me illustrate both how these presuppositions operate and the limits of their resolving power.

Adjudicating Cases.
Administrative adjudicators in the U.S. make millions of decisions annually and across a wide range of administrative functions. Often these adjudications involve claims of right which must be determined on a record after opportunity for hearing and argument. Opportunity for appeal of these adjudicatory decisions, either to a specialized tribunal or to general court seems, to the modern legal mind, non-problematic. Reviewing lower tribunals is the work that appellate courts normally do within the general civil or criminal law.

Yet review of administrative adjudication raises immediate concerns: What scope of review should reviewing in courts exercise, and what remedies should they apply in the case of legal error? To what extent should courts be involved in restructuring the processes of administrative adjudication as against merely ruling on the legality of their outputs. To what extent should the courts rely on standardized administrative routines as guarantors of regularity in high-volume, fact-based adjudications? And, what deference should be paid to the judgments of administrative adjudicators in cases that "make law" as well as apply it. In answering many, if not most, of these questions courts confront tradeoffs between or among legal, political, and managerial accountability.

It seems clear, for example, that much judicial "deference" to administrative adjudicators is based upon the perception that administrative adjudication makes policy as well as applying law. As part of its accommodation to the American administrative state in the New Deal era, the United States Supreme Court famously deferred to the judgment of the National Labor Relations Board concerning whether employees needed the protections afforded by the National Labor Relations Act. It did so through the lawyer's device of finding that the determination of "employee" status was a question of "fact" within the ordinary experience and expertise of the Board.[9] The Court has also made clear that the Board has the choice of making policy through either adjudication or rulemaking and that the Board's choice in this matter will be reviewed only for the most extreme cases of abuse of discretion, that is, effectively never.[10]. In short, these decisions suggest that policy is for the Board subject to accountability to the political branches for the shape of labor relations law. And, because the Board makes policy almost exclusively through adjudication, respect for the proper role of political accountability limits the reach of legal accountability for adjudications through judicial review.

If this were the whole story, it would be nicely counterintuitive, that is, political accountability trumps legal accountability even where one would expect the latter to be most robust. Yet, the story is not so simple. The political branches have responded to the judiciary's self-limitation by suggesting that they expect courts to engage in more searching review of Labor Board determinations.[11] And, as Labor Board policies accrete and are judicially approved, what is their status? Are they

precedents that now bind the Board in future adjudications? Or, does the Board remain free to alter policy as it perceives shifts in social and economic context? The answer seems to be the former.[12]

These developments almost turn the story on its head. Well-informed commentators have argued that judicial review has seriously impaired political accountability for Labor Board policymaking both by granting the Board discretion and by restricting it.[13] By giving the Board *carte blanche* to use adjudication as its principal policymaking device the courts have allowed the Board to bury policy in the factual complexities of individual cases and to, thereby, render political oversight virtually impossible. And, by demanding Board adherence to "precedent", the courts have deprived the Board of the flexibility to be politically responsive. In short, where judicial review should be expected to be most sure-footed and non-controversial, in reviewing administrative adjudication, the judiciary is accused simultaneously of abandoning serious legal oversight while limiting the Board's political accountability.

To take another prominent example, the Supreme Court has deferred extensively to the judgments of the Social Security Administration concerning the structure of its adjudicatory processes.[14] Here deference is not so much to administrative policy choice, subject to political accountability, but to managerial judgments about the necessities of administration. The Court has relied explicitly on the circumstantial reliability of internal administrative routines that make individual adjudicators accountable and administrative processes "fair" to claimants.

Yet, the Court has found itself intervening in other public benefits processes that it found less reliable and regularized.[15] In doing so the Court substituted its own judgment for the administrators' concerning the types of adjudicatory process necessary to produce accurate and reliable decisions. Courts have also suggested a willingness to intervene in the managerial efforts of the Social Security Administration where those efforts might impair the "independence" of administrative adjudicators.[16]

In many ways the Supreme Court's attempt to find an accommodation between citizen demands for individualized hearings concerning their rights and the necessities of mass administrative justice are laudable. In a liberal democratic regime of the 21st century, the citizen's rights are often held in the fragile currency of some form of state-based concession: professional licenses, access to education, pension rights, and so on. If the citizen is to be treated as an independent end, not merely a means of effectuating state policy, then surely these rights must be attended with forms of legal security that make them defensible in the face of bureaucratic error or corruption. Individualized hearings with demands for proof and a judgment on the record are a major bulwark against state oppression.

Yet, individualized hearings are wonderfully anti-bureaucratic. They interrupt regular routines, require the expenditure of disproportionate resources on particular decisions, and risk defeating the goals of programs designed to promote the general

welfare. Hence the delicate balancing act between defending individual rights to particularized proofs and judgments and deference to administrative judgment concerning how hearings might best be structured to maintain administrative capacity.[17]

The point here is that the necessity to balance "legality" against "administrative necessity" puts reviewing courts in an almost impossible position. To defend rights they must insert procedures into bureaucratic regimes with little or no capacity to judge what their ultimate effects might be. And, reliance on administrative necessity may easily turn out to be misplaced where the institution doing the relying - the court - has limited insight into the dynamics of administration.

Thus, for example, in a famous case in which the Court deferred to Social Security Administration's assurances of the circumstantial reliability of its data, commentators have suggested that the Court failed to appreciate both the nature of the decision that was being made at the administrative level and the degree to which the data relied upon bore on the ultimate determination.[18] Indeed, had the court been able to do a managerialist audit of the reliability of the system it was affirming, it might have been alarmed at the apparent inconsistencies across deciders and the astonishingly high rate of victory by petitioners who appealed their decisions.

On the other hand the Court's willingness to intervene to protect the independence of administrative law judges, who hold formal administrative hearings in the American system, may well have undermined managerial efforts to assure the consistency and accuracy of administrative determinations. And, where the Court forcefully inserted rights to hearings in welfare administration, this victory for the "common law ideal" of individualized days in court may have dramatically and unpredictably shifted the basic priorities of welfare administration. Assuring "rights" through adjudication may have contributed substantially to the loss of the program's capacity for client services and have shifted managerial effort from the pursuit of professionalized social services to the defensibility of income eligibility determinations.[19]

All of these critiques of both deference and intervention are, of course, contestable. But they illustrate my basic point: Even in the realm where judicial review seems most appropriate, the review of, and defense of, administrative adjudicatory processes, legal and managerial accountability, like legal and political accountability, are strongly competitive. More importantly, because managerial accountability often supports the same values of accurate adjudication that are pursued through the assertion of legal rights to hearings and review, missteps undermine not just managerialism, but the purposes of judicial review itself.

Rulemaking.

Modern administration entails the creation of a host of subsidiary norms, that is, rules, bulletins, memoranda, guidelines, manuals, and other documents that give more concrete meaning to the terms of general statutes. Techniques for generating

these norms vary enormously across legal systems. Some treat administrative rulemaking as quintessentially political and subject only to regimes of political accountability. Yet it is difficult to keep the law from creeping in, particularly in "presidential" or "separation of powers" legal systems like the American one. Because administrative jurisdiction and authority flows almost exclusively from statutes, political control of administrative discretion by presidents is always subject to the question, "Was that act authorized by law?".[20] And legislative attempts to direct administrative policy free of presidential interference may be viewed as unconstitutional in regimes that treat the President as the Chief Executive Officer.[21] Even political accountability has a legal structure that can be used to mount legal challenges in court, and this is but the tip of the legal iceberg.

Recognition that statutes do not necessarily determine policy choice and that political controls over administrative discretion may be weak have, in the U.S., lead to micro-political controls on administrative policy making. Harking back perhaps to Athenian democratic ideals, American administrative law gives any person a right to participate in agency rulemaking processes. Moreover, Congress has often insisted that judicial review be available to determine whether any administrative action, including general rules, is "arbitrary". These process guarantees and provisions for judicial oversight have produced substantial incursions into administrative policy making, even when policy is announced as a general norm or "rule".

That a Congress that finds itself unable to give administrators crisp statutory instructions might be tempted to rely on judicial review as a means of reigning in rambunctious administrators is understandable.[22] But, the American Congress' penchant for providing for immediate review of agency regulatory pronouncements has created a mini-crisis of accountability by thoroughly confusing political and legal accountability regimes.

A court faced with the question whether an agency rule is "arbitrary" is in reality faced with a political question: Has the agency's policy judgment been so bad that it should be nullified? That sort of substantive policy issue seems an issue of politics, not law. But, the statutes mandating judicial review demand a "legal" answer. And, the courts have responded by "proceduralizing" arbitrariness to make judicial review of rules legally manageable. The basic technique is to model the rulemaking process on the process of adjudication. Adjudications may be arbitrary in two senses, either substantively, because the facts of record do not justify the agency's conclusions, or procedurally, because participants have not been given a fair opportunity to participate.

American courts have taken essentially the same approach to rulemaking processes. Attempting to the extent possible to avoid the substantive, and inevitably political, judgment of whether agency policy makes sense, courts pursue related "procedural" questions of the adequacy of notice, the responsiveness of the agency to relevant comments of participating parties, the adequacy of the agency's explanation, and the exis-

tence of facts in the "record" that would justify the agency's findings. The result has been to preserve the law-like nature of judicial review, but to impose severe, sometimes insurmountable, burdens on administrative policymaking[23]. In recent years the Supreme Court has attempted to redress the balance, in part, by giving deference to agency interpretations of their own statutes. This deference is premised on the political proposition that the agencies are the delegates of the legislature who have been authorized to "make law" by their interpretive regulations.[24]

The result of making rules reviewable while asserting deference to policy choice has been a peculiar and uncertain jurisprudence. Peculiar because it seems to give judicial deference to agency interpretations of *law* while immersing courts in the often technical *facts* in the rulemaking record. Uncertain because it has given important legal armaments to obstructionist element in the agencies' regulatory space. Every rule is contestable on a host of possible legal grounds and a reviewing court's reaction to these complaints is often unpredictable. This provides strong incentives to seek review and strong disincentives for agencies to engage in rulemaking. The result is that rulemaking has languished and much administrative policy making has been driven underground. And lack of transparency tends to undermine political accountability.

One of the more important American cases on judicial review of administrative action provides some important insights into this uneasy relationship between legal and political accountability. *Motor Vehicle Manufacturers Association of the U.S., Inc. v. State Farm Mutual Automobile Insurance, Co.,*[25] involved the legality of the most important safety rule ever adopted by the National Highway Traffic Safety Administration (NHTSA) - its requirement that all vehicles be equipped with passive restraint systems (either automatic belts or airbags). The regulation had been twenty years in the making, a regulatory history that demonstrates starkly the unpredictable interactions between legal and political control of administration.[26]

The rule was first promulgated in the late 1960s, but was immediately derailed by a judicial determination that the agency's engineering specifications were inadequate. That ruling was both questionable and unnecessary, but sent the agency literally back to the drawing boards. NHTSA then produced a stop-gap measure using a different technology – ignition interlocks—to prevent the use of automobiles unless the passengers had attached their seatbelts. This second attempt ran afoul of the political process. Congress received thousands of complaints about the requirement and passed legislation to repeal it.

A change of presidents then put passive restraints on the back burner in an administration that was more interested in promoting automobile sales than regulating their safety. The rule languished until a pro-regulatory administration revived it and repromulgated it. But, the effective date for compliance outlasted that administration's mandate and a less enthusiastic administration decided to require only a "demonstration project" involving a few thousand vehicles. That administration again

passed from the scene and the rule was repromulgated, only to be rescinded by the next deregulation-minded president.

If this sketch tells us anything, it is that the issue of passive restraints was a highly political question, not a mere exercise in technocratic safety engineering. The rescission set the stage for the *State Farm* case in which various automobile insurance companies challenged the rescission of the rule as having insufficient basis in the record. On this score, they were surely correct. The agency had spent twenty years compiling a record to support the rule, and the information supporting its rescission was quite thin. The Supreme Court, therefore, invalidated the rescission as being inadequately rationalized.

This much is clear - congresses and presidents asked whether the rule was wanted. The courts asked a quite different question, whether it was adequately supported by the record either for promulgation or repeal. And, while the Supreme Court in *State Farm* recognized that the repeal of the rule was almost certainly the result of a change of administration, and therefore, a change of policy, that policy ground was insufficient to sustain the rule. Having "legalized" the review of rulemaking, by translating it into a rational process of weighing evidence compiled in a record, it was simply not possible for the defendant administrator to tell the truth and be upheld. For the truth was something like this: "I represent an administration that was elected campaigning on deregulation and regulatory relief for the automobile industry. There is some question about the safety benefits of the passive restraints rule, and given my administration's political ideology, we act by a simple motto: When in doubt don't regulate'."

When told in this way the *State Farm* story has a simple lesson: seen through the lens of judicial review, administration is apolitical. Indeed, administration must be made apolitical in order to subject it to legal accountability. And, to this degree, *State Farm* is quite consistent with the Supreme Court's constitutional jurisprudence in which the Court has been prepared to place relatively stringent limits on the powers of both Congress and the President to control administrative policy. Indeed, the Supreme Court's separation-of-powers jurisprudence so muddies the waters of the reach of presidential and congressional control over administrative policy making that the question of whether administrators are politically accountable to the President or the Congress has no straightforward answer.[27] In part, and through certain techniques, administrators are answerable to both. But whether this reinforces or destroys political accountability is hard to judge. Many would say that an agent who must satisfy two principals is in a good position to avoid satisfying either.

Judicial review has therefore, to some degree, reinforced the independence of administration from politics and political accountability. But, political institutions that are electorally accountable for government action are unlikely to give up their capacity to control governmental actors without a fight. Deprived of authority to

dictate or veto administrative policy choices, both presidents and the congress have attempted to reassert political control over administration by the creation of "managerialist" techniques.

Virtually any major federal, administrative in the United States action must now be attended by a host of analyses that describe in great detail the proposal's effects on the environment, on the structure of American federalism, on the paperwork burden on American firms and citizens, and on small entities both public and private, as well as providing an analysis of the costs, benefits and alternatives to the action proposed and the means by which all data used by the agency in its policy-making has been vetted for its scientific quality.[28] These analyses are subjected to review and audit by various "super agencies" in the executive branch and by Congress. Negotiations about the adequacy or soundness of these analyses thus becomes a pathway for reasserting political control by elected officials, particularly the President.[29] As we noted earlier, the membrane that divides "managerial" from "political" accountability may be porous.

Moreover, because all of these analyses become a part of rulemaking records, they are also a part of the factual predicate that is available to a reviewing court when determining whether the agency's behavior is or is not "arbitrary". The consequence, once again, has been to reinforce legal accountability through judicial review. Not only may outside parties use judicial review to defeat or delay administrative action that has not satisfied various analytic requirements, courts have held that the Office of Management and Budget, which oversees most of these "impact statement" regimes, may not use its oversight powers to unreasonably delay agency action.[30] Political control, in a managerial form, is thus made legally accountable.

Administration.

Government officers also carry on a huge array of managerial tasks that have little to do with either deciding cases or generating rules of conduct. They manage public lands and state-owned enterprises. They promote the exploration of space and manage the money supply. They build or subsidize infra-structure development, police the borders and attend to the national defense. They set agendas and supervise personnel.

Much of this activity is free from judicial or legal review. In the words of the American Supreme Court there is "no law to apply". These administrative judgments are often judgments of economic or engineering feasibility, political importance, and administrative capacity. Yet, strangely enough, the leading case on the presumption of judicial review of administrative action in the United States is a case involving infra-structure development – the building of highways.[31] And one finds courts routinely reviewing Corps of Engineers' water projects and Department of Interior leasing arrangements on public lands. A closer look reveals that most of these cases are the

result of cross-cutting statutes, particularly statutes concerning environmental protection, that attach non-managerial criteria to administrative routines. These requirements have been inserted in the statute books to broaden the vision of mission-oriented administrators. And Congress has relied upon the courts and private litigants as a means for ensuring attention to these broader societal values.

But, the results of "legalizing" management have not always been benign. The *Overton Park* case, the modern administrative law case that most dramatically established the principal of presumptive judicial review of administrative action in the United States, provides a cautionary tale.[32] The plaintiffs were a group of citizens unhappy about the routing of a highway through Memphis, Tennessee. Because the route chosen included the taking of some park property, the plaintiffs seized on the language in the Federal Aid Highways Act that required (1) that highway engineers avoid the use of park lands unless there were no "feasible or prudent" alternative and (2) demanded that they use "all possible planning" to minimize the damage to park lands ultimately disrupted by highway construction.

The defendant, the Federal Highway Administration, had treated the planning and building of Interstate 40 through Memphis, Tennessee, as an exercise in managerial administration. It had worked with the Tennessee Highway Department and multiple local and state planning bodies to develop a route that satisfied the need for traffic movements, subject to the constraints of local land use policies and the budget available for highway construction. The project had been ongoing for many years with multiple reanalyses and reassessments of the soundness of the plan from engineering and fiscal perspectives.

The process was also highly political. The routing of the interstate highway had been a major political issue in Memphis for nearly a decade. Local elections had been fought on the basis of that issue and the people of Memphis seemed to have spoken in favor of a city council that was committed to the project. On the basis of all this engineering, fiscal and political information, the Federal Highway authorities had determined that the chosen route through Overton Park was the only feasible and prudent one.

In the crucible of judicial review, the multiple, incremental decisions of highway construction, filtered through both technical and political processes, looked quite different. The plaintiffs urged that the Federal Highway Administration had simply misunderstood the words "feasible and prudent" in the statute. They urged, and the Supreme Court agreed, that the Congress had meant to provide strong protections for park land against the encroachments of road building. In the Court's view the administrator needed to find, in order to justify his decision, that any other route than the route taking park land would be "uniquely difficult" because of community disruption, or engineeringly impossible. Moreover, the Court refused to accept the administrator's explanations, offered in litigation affidavits, in response to the

plaintiff's lawsuit. In the Court's view the administrator had to "make a record" that justified his decision, not simply provide "post-hoc rationalizations" in the context of litigation. The notion that the lawsuit was misplaced because highway building was not appropriately subjected to judicial review was brushed aside. In the Supreme Court's view any time there was "law to apply" a court could be called upon to determine whether it had been properly applied.

On remand to the trial court, and after 128 days of testimony, the trial court found that the history of the project as presented in court did not satisfy the Supreme Court's "uniquely difficult" standard for choosing a park land route. The question was remanded to the Federal Highway Administration which declined to continue funding for the project. The federal administrator was then promptly sued by the State of Tennessee which claimed that if there were feasible and prudent alternatives to the park land route, the administrator was obliged to specify them and fund the project in that location. This put the administrator in a quandary. Federal and state officials had spent a decade devising a plan on the basis of their judgment that there were no feasible or prudent alternatives. There was no administrative record upon which a determination of an alternative route could be premised. Once again the state and local officials went literally back to the drawing boards.

I describe this as a cautionary tale because the judiciary's intervention has obvious effects on political and managerial accountability for road building. On the political side, the Court's *Overton Park* interpretation of the Federal Highway Act shifted authority strongly away from local communities, who are most effected by such endeavors, and toward national elected officials whose priorities may be quite different. The balance of benefits and costs between park lands and highways is to be decided by federal administrators under national statutory standards that give no obvious weight to local political preferences. The inter-governmental processes of political accommodation that surround joint federal-state-local projects is subordinated to the hard edges of the law.

The decision also imagines a managerial environment that highway engineers may find quite unrealistic.[33] The Court seems to assume that highway building involves ratio-deductive thinking in which facts are gathered, decisions are made based on the application of technical methodologies, and can be rationalized in straightforward logical fashion. The informal and iterative process of professional consultation and craft judgment is not captured by this picture. Moreover, if administrators want to avoid lengthy trials about their engineering decisions, the *Overton Park* case implicitly instructs them to bureaucratize the process in ways that create records suitable for judicial review. How that effects the real processes of road building is anyone's guess.

In short, subjecting these sorts of decision to judicial review implicitly makes real choices about what sorts of accountability regimes are appropriate for ensuring

managerial responsibility. The progressive logic of judicial review, if there is law, then there is review, obscures these choices as much as it illuminates them.

One should not take away from the *Overton Park* case, however, the idea that managerial discretion has been eliminated from American administrative law. American courts clearly recognize that agenda setting is one of the most critical aspects of administrative management. As a consequence, courts have been reluctant but not entirely unwilling, to invade administrative enforcement discretion or to attempt to set agency regulatory agendas.[34]

Perhaps the most important thing to notice about these limitations on judicial review of managerial discretion has to do with the way that insulation from legal accountability may create imbalances in administrative incentives. For while it is presumptively the case that an agency adjudication or agency rulemaking will be subjected to judicial review at some point, precisely the opposite presumption applies to agency failures to act. Agency agenda setting about either policy making or enforcement is an aspect of managerial discretion that in the American vernacular is "committed to agency discretion by law". This means that where political and administrative accountability regimes fail to mobilize administrative energies, judicial review will take up very little of the accountability slack. The modern political world is planted thick with laws, but the beneficiaries of those laws can only occasionally rely on the judiciary to assure that they are enforced.[35] In the American administrative state legal accountability thus has a decidedly liberal democratic character. State action that potentially invades individual freedom or impairs individual rights or interests is presumptively subject to judicial review. Administrative inaction that fails to protect the weak from the strong, or diffuse from concentrated interests, is presumptively not reviewable.

Judicial review in the U.S. thus seems to play out a political project of accountability for official action that responds to the peculiarities of the American political culture. It is perhaps not too much to suggest that judicial review in the United States is structured to pursue Thomas Jefferson's famous aphorism that "that government governs best that governs least." Public law rights in the United States follow the political culture's preference for insuring "negative" rather than "positive" liberty.

Reflections on Institutional Design

Every democracy struggles to keep a workable division between law and politics. If the citizens' legal rights are subject to the political whims of the rulers, the fundamental presuppositions for democratic governance are erased. The citizen cannot be the pawn of the state and simultaneously the source of its authority. Judicial review of administrative action is a crucial aspect of this democratic project. If officials are not subject to the law, then democracy is a sham. We simply elect our dictators.

Democracy struggles as well to balance the demands of political responsiveness and governmental competence. In the modern world that has often meant separating governance from electoral politics. Indeed, in some significant sense, electoral politics cannot produce responsive government unless it is harnessed to technically competent administration. And incompetence is politically dangerous. As has proved so common in the past, incompetent democracy will give way to authoritarian regimes that promise in the hackneyed phrase "to make the trains run on time".

Here again judicial review has a role to play. Elected officials cannot monitor the far flung activities of the modern administrative state. But citizens affected by official action can do so in part through the processes of judicial review. For, administrators called to account in court to justify their actions according to law are also being called to account for the technical competence of their actions. Requiring factual predicates for action and reasoned explanations of decisions ensures that administrators, in Weber's famous phrase, "Exercise power on the basis of knowledge".

I do not, therefore, deny for a moment the role of judicial review of administrative action in maintaining politically responsive and technocratically competent governance. This paper has emphasized, however, the potential paradoxes and tradeoffs of making administrators accountable to law. For judicial review both supports political accountability and impairs it, demands administrative competence and undermines managerial capacities. Moreover, the way that judicial review will interact with other accountability mechanisms, the political and the managerial, are often unanticipated and unpredictable. The task of institutional designers is therefore not to get the balance right once and for all. It is instead to understand the project for what it is, a project of democratic experimentalism. Democratic governments would surely be incompletely accountable without effective judicial review. But, if "accountability" is the goal, reinforcing or extending judicial review will not always be the answer.

NOTES

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15 *See*, e.g, Goldberg v. Kelly, 397 U.S. 254 (1970).

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Jerry L. Mashaw Sterling
STERLING PROFESSOR OF LAW AND MANAGEMENT YALE UNIVERSITY

THE TRADITIONAL DIALOGUE BETWEEN LAW & ECONOMICS

José Reinaldo de Lima Lopes

The purpose of this paper is to discuss the possible compatibility of legal and economic reasoning. I assume that law and economics are two different subjects and have been so treated in the civil law tradition for quite some time now. Economics has developed in the last two centuries as a field, although it originally grew out of ethics, or political science (*politica* and *policia*) and in this respect it gained autonomy from a larger field of knowledge: practical philosophy. Law also developed from the same field, but it has a much longer career, that could be traced back at least to the XII century, in Bologna in the case of Western law. Contrary to what happened with economics, law never developed any mathematical or abstract model, in spite of the efforts made by Leibniz.

The discussion I am suggesting has its context in a constitutional framework and an economic circumstance: it takes place in a legal system whose highest or primary rule is a written constitution of a welfare democratic state (*estado social de direito*), and it is contemporary with the rising of a global economy. Another important part of its circumstance is a given and strong legal tradition. Legal thought in Brazil has a fairly established tradition of almost 180 years. Law does not grow on trees; it grows on collective imagination and collective imagination is not to be taken lightly. This discussion, therefore, takes place in a historical and existing legal system, in which people (ordinary citizens and legal practitioners) already act, exist, believe in things and behave accordingly. Rules do exist and have been used for a long while now. The background legal culture of this paper is one where the liberal tradition of strong protection of private interests is dominant, as

has been revealed by the research of Castro on the Supremo Tribunal Federal (**Castro** 1977).

A general background assumption of this paper is the belief that even if economics has not been usually acknowledged as an important part of legal practice, its practical character as well as the general applicability of its mode of reasoning in certain practical matters have provided rules that jurists usually apply. Therefore, state regulation of the market comes not as a total novelty in terms of legal reasoning. In fact we can show a long series of examples of economic rationality living within the legal field. These examples however frequent and daily as they may be, are not the ones that shape the minds of legal practitioners. This paper will try to show how economic reasoning may enter into the law. But in so doing it will also acknowledge or suppose that legal reasoning keeps its autonomy and in certain issues economic rules will not be allowed to override legal considerations. Finally, then, the paper assumes that the economics may not play the role of the supreme practical philosophy.

I assume that such a task is relevant in Brazil as legal scholarship, legal practice and court decisions have tended to equate economic regulation with undue interference of the state in private freedom or with unacceptable use of economics to decide legal matters. Tension has risen among courts of different levels with some accusations that higher courts make political judgments, whereas lower courts make technical (legal) decisions. This sort of political confrontation is sometimes fueled by legal scholarship that underestimates the analysis of what legal reasoning really does and allows to be done.

The paper is divided into three parts: a first part deals with the differences between legal and economic reasoning, by assuming that both disciplines diverge in terms of the meaning of actions each of them assumes as a given. The second part will proceed historically, providing a short series of examples of the existence of economic concepts in legal practice and affirming the need to restore the analytical distinction between commutative and distributive justice. A short concluding section will analyze a possible research agenda for the doctrine on regulatory agencies and their possible conflicts with the judiciary branch.

1 Ideal types and reasoning

1.1 Result-oriented and rule-oriented action

Meaning and purpose are important concepts in dealing with human action. When we mention purpose, we assume that a given behavior is not simply the result of blind reaction. It involves some sort of choice, intention, etc. When we mention meaning we assume that the person will be able to give reasons. Meaning and purpose help us answer the question "why?" We can either answer "because…" or "in

order to…" The question "why" in this sense requires that its answer be given in terms of understanding. "Understanding is equivalent to: the interpretive apprehension of the meaning or connection of meaning". (**Weber** 1977, 9)

The answer to the question "why" could be given at different levels: (1) first it could give us a hint, or an apprehension, of the actual meaning of a given action (from a historical point of view: the actual intention and the actual understanding of a given and individual subject in a given circumstance along with her fellow subjects, etc). (2) Second, it could be answered by a general consideration, so it would be like a summary or an average account of what "people" usually do (an empirical generalization). (3) Third, the answer may be given from an ideal point of view, so that it takes the subject (the individual) not as an actually existing being, not even as a general (empirical average) being, but as *typos*. Of course, I am just reporting Max Weber's famous assertion about the differences between an "ideal type" and an "empirical generalization." This is a helpful way to start, as I am convinced that in this respect Max Weber was right. Law and economics, as two different disciplines, deal with two different meanings and purposes of human action.

Weber says that in contemporary times, it was economics that best developed this conceptual tool (the *ideal type*). Economics assumes just one isolated aspect of human rationality and action, and it develops its theory and the laws of pure economics out of this assumption (this type). It converts any human action in its own terms, it constructs one instrument of commensurability of actions (money – the *universal measure of goods*), and it proceeds to analyze "this special form of human behavior, if it were taken thoroughly seriously and devoted to one purpose, without any disturbance either from mistakes (errors) or affections, aimed at one exclusive end (the economic end). But the actual action only in a few cases (the stock exchange), and even then only in an approximate way, happens in the same way as it was conceived in its ideal type." (**Weber** 1977, 9) Economics has gained enormous prestige within the academy even though its capacity to give a secure account of what will happen in the future remains fairly limited. It may work better in certain fields, but even then, all it can say is that things will happen this way, *caeteris paribus*. If people invent new modes of credit, if new ventures are created, if a new technical discovery is made, if the organization or division of labor change, if… then, it is rather possible that things will diverge slightly or greatly from what the ideal type suggested.

If the ideal type of economics is a certain form of rationality, and if this rationality gives meaning to actions "from an economic point of view", it is a good start to assume that human action and legal rationality can be accounted for "from a legal point of view". My idea is that law too has developed an ideal type and has been rather successful in using it. Its present lack of prestige is due to a variety of factors,

but I will not go into this here. I will rather try to recover what the specificity of law is, to further discuss how law and economics merge (if they do) in the legal apparatus of economic regulation. If you would excuse my going back some two thousand years ago, we will find this point of view explicit in Roman law, and then re-elaborated throughout medieval law: "the force of laws is either to command (oblige), to prohibit, to allow (permit), or to punish" (D. 1.3.7 – *legis virtus haec est imperare, vetare, permittere, punire*). So the legal point of view is essentially in its quintessence, the point of view of "following a rule". Law's ideal type of rationality is not obtaining some "good", unless "good" is defined in such a general way that economics loses its classical specificity and becomes a general concept. But then we should go back to the tautological definition of good that leads us back to ethics or practical philosophy as it was understood until the XVIII century, in which case we would have come full cycle for economics: leaving ethics (since the physiocrats and Smith) and returning to it (with Becker, as put by **Pacheco** 1994, 77).

In designing an ideal type of law the two greatest legal scholars of the XX Century took two different views. For Hans **Kelsen**, the ideal point of view of following a rule should be constructed from the perspective of the subject who wants to avoid punishment. For Herbert Hart it was the subject who wanted to do the "right thing". Whereas for Kelsen the ideal type of the legally rational man would ask "how can avoid punishment?", for Hart the ideal type would ask "what do I have to do to be a law abiding subject?" But both had in mind the same rationality: even if for different "reasons", the ideal type is the reason of one who is trying to "follow a rule".

Ethics is another field of knowledge in which following a rule is the most prominent feature. This is why jurists in the course of Western history have always inquired into the differences and similarities of legal and ethical rules. One tradition within ethics, whose lineage is traced back to Aristotle, says that ethical rules are those that make men fully happy. Another one, expressed in German idealism, states that ethical rules are those whose obligatory force derives exclusively from the a priori or transcendental "sense of duty" determined by the principle of universalization. In either case – law and ethics -the idea of following a rule is an essential one: rules provide both a guide for action (from the point of view of who has to act and make choices) and an evaluation tool (from the point of view of the very subject or his fellow human beings) to criticize one's choice. And this holds true for both law and morality. That is the point made by Aquinas when saying that law (*lex*) could be a measure in two different senses: first it was a measure for what should be done, as an architect has a measure to design his project; secondly it was a measure of what had been done, as when the architect finishes his work, and then verifies its results. It was, he said, a measure for action and for the product of one's action.

However, if we intend to make a comparison between economics and law, the rationality in both cases is different in the sense that decisions will be assessed

(measured or criticized) in the realm of economics by "efficiency", whereas decisions or actions in the realm of law will be assessed by the criterion of "legality". That is, efficiency, in itself, will not be a full criterion of legality. It may be a lot more efficient to kill a part of the population, but laws tend to prohibit mass extermination of the poor, the sick, the undesired, and the ethnically diverse. Criteria of efficiency and cost benefit cannot be called as reasons to act in all circumstances. Sometimes legal reasoning is a limit to economic reasoning: no matter what the cost is, certain things are not done.

Authority in law provides an important criterion that differs from efficiency. You cannot explain (give reasons) in legal terms except by referring to some authority: impersonal and burocratic, traditional, ideal and transcendental. In the long history of Western legal tradition, different authorities were accepted as foundations of a legal system. The civil law tradition has developed sophisticated doctrines to determine what the *sources* of law are. Sources of law change. Different sources of law are actually different authorities. Why do you do this? Because the law tells me to do it. That is a perfectly sound answer, in legal terms, even if the specification of "what the law actually tells" is another incredibly large field of practical and academic discussion. What is the law here and now? Well, constitutional customs (the decisions of the Supreme Court, for an American citizen); a written text (and its doctrinal meaning) for a civil lawyer; the tradition of our people, for another group, and so on. But in the end, everyone will give an answer referring to some authority, even a simply moral authority (as it has been the case in international human rights law until recently, or – as I understand it – in Dworkin's account of jurisprudence).

Kelsen's ideal type is looking for an authority, and the authority she will find is, at the very end, the one allowed to impose a punishment. I will not go into the details of the philosophical nature of the "authority" in Kelsen. Suffice it to say that it is not a 'de facto' power (*potentia*), as some usually assume: it has to be a legal power (*potestas*).[1] Kelsen insists that his concept of validity is not empirical. In the case of Hart, authority too is objectified in the "rule of recognition", whose logical function is exactly that of providing an authority, a "source" or a "principle" for any legal argument. In Hart's case too, he refuses the accusation that he is a "plain fact" positivist, because the rule of recognition is not equal to empirical power.

It is fairly easy to take "authority" for an empirical authority (a person, an institution). It is also easy to take a rule as an order, in which cases the idea of rule is associated with a command given by someone. But there is more to it – following a rule may be more than just obeying someone's orders. There may be some logic to the idea of following rules. This logic in legal reasoning authority suffers from a general "constraint of formal justice" (**MacCormick**) or a general constraint from the "principle of unity and equality" (**Canaris**), or "adherence to principle" (**Rawls**), or

"static justice" (Agnes **Heller**). This means that the very idea of a rule implies limits. **Wittgenstein** has a clarifying insight in his *Philosophical Investigations*. In discussing the idea of following a rule, he says that only someone who has grasped the idea of equality is capable of grasping the idea of a rule (and vice-versa). This is why examples always have to refer to types, not to things that happen only once: they express rules. Maybe this is also the idea found in the long tradition of Roman law: "laws are not made for things that happen only once" (D.1.3.3 and D. 1.3.4 – *ex his quae forte uno aliquo casu accidere possunt iura non constitutur*).

The very idea of law and rule imply the idea of equality. And the idea of equality implies that in like situations and in like cases, the same criteria should be used: the individual should act according to the same standard in every similar situation and different standards will only apply when differences are shown to be substantial. Now this is, of course, the concept of justice: "treat equal cases equally, and treat different cases differently". Justice is equality, and inequality implies both injustice and non-consistency. There is a sort of logical flaw when differences are not respect and there is a logical flaw when equality is not respected. In a way it is a sort of absurd (as Hobbes puts it, getting the idea from the late scholastics, especially Luis de Molina, probably): in formal logic, reasoning is impossible if the principle of identity and non-contradiction is not applied. The same thing is true when legal reasoning does not "follow a rule".

Canaris is very clear about it:

> "The internal order and unity of law are far more than just scientific presuppositions of legal methodology; they belong above all to the most fundamental ethic-legal exigencies and are finally based on the very idea of law. Thus, the so-called requisite of order is a direct result from the well-known postulate of justice, to treat equal cases alike and to treat different cases differently, according to their differences. Both the legislator and the judge are bound to take the values seriously and think them thoroughly, up to the end, with all their individual consequences and avoiding their application only with justifying reasons, i. e., for substantial reasons: in other words, they are bound to act adequately. Rational adequacy is, as it has been said, the typical 'order' in the sense of a system, and therefore the rule of value adequacy, drawn from the principle of equality, is the first decisive sign for the use of systematic thinking in legal science, which is correctly explained by Flume, following Savigny, when he says that it is the legal consequence interiorly presupposed."
> (Canaris 1996,18)

In this respect, the very idea of law implies the idea of justice from the logical point of view. I am not dealing here with the application of the principles of justice in actual situations, but rather with the logical idea of justice, which is that of equality.

It is doubtful if this idea of equality, rule and justice plays the same central role in any other academic discipline within the realm of the "social sciences". When it does, it implies that the scholars of the field are supposed to use certain standards – that is, that they are bound to be consistent in producing their findings. But they are not interested in the establishment of the internal adequacies in the phenomena they study. This is due to the fact that they do not approach their subjects with a basic "practical" purpose.

A sound economic reason, even when based on belief in someone's academic expertise or financial power, does not necessarily really on authority and rules in the same way as law. Economic reasons will finally say: "because this is more "economically sound" (efficient, cost-effective, etc). Of course I am oversimplifying the issue and totally ignoring the discussion within the economic field itself. My purpose here is just to insist that law and economics have operated on different grounds as far as conceptual frameworks go.

If the assumed rationality of economics is taken to be an empirical generalization or an ideal type, cases of non-conformity with it may generate the idea of a deviant rationality, in which case, someone who is "in charge" should try to correct the deviant rationality. Public authorities, business managers may then try to educate, correct and direct behavior which is not "rational", that is, which does not seem to be able to insulate certain spheres of action from the other spheres of action. When, for instance, some one takes bounds of affection or blood relations into account instead of taking exclusively "economic" factors, this sort of behavior is deviant, from the modern point of view. But then, assertions such as these are definitely assertions of an ethical nature. [2] In fact, the practical side of economics may imply that "irrational" behavior can also be corrected.

Economic reasoning, as practical reasoning, is (a) forward-looking and (b) takes cost efficiency as a standard of rationality. The fact that it is forward-looking means that it is not interested in "passing judgment" on what has been done, not in the sense that whoever has done it "must" be "punished", or must "pay back" what has been done. Economic reasoning takes the past into consideration in order to "learn" from it. It does not work in terms of "imputation" (**Pufendorf**). This is a fairly important trace of human agency so it but the tradition of legal reasoning in the last three hundreds years has not concentrated on this particular aspect, which had been a part of legal scholarship in other times.

Economics takes the agent's response to her environment to be rational when it satisfactorily considers costs and benefits and finally chooses the one that results in greater benefits and lower costs, as the empirical limits of the situation will allow. This is the same type considered by John Rawls "the concept of rationality must be interpreted as far as possible in the narrow sense, standard in economic theory, of taking the most effective means to given ends." (**Rawls** 1992, 14) Of course, what

are the costs and what are the benefits expected remains a matter of controversy, but the reasoning, the model or the form of the deduction remains valid.

This is naturally very different from a rationality that is backward looking, like that involved in retributive justice, and also different from one that has to reason from "counter-factual" premises. That is one typical case of law. Law is an instrument of deciding on what is "right" or "wrong" from a counter factual point of view. Regularity does not play any part in normativity. Norms are necessary exactly when regularities will not lead to "satisfactory" results: norms are needed exactly when revenge (*vendetta*) will make life impossible in civil society. And law is typically used with a backward look: this is typically the case of adjudication.

If we consider the classical philosophical tradition it is clear that forward looking, in order to decide what to do, and looking backwards to decide on the "goodness" of what has been done are at the center of Aristotle's analysis of the uses and functions of rhetoric as a form of reasoning. Rhetorical techniques are standards of correction of the use of one's reason in dealing with what is contingent, not necessary. What is "contingent" (that is, merely *possible*) either will happen in the future, or has happened in the past. In both cases, he says, problems of "evidence" are at the very core of the techniques of rhetoric. In order to pass judgment on what happened we need to know the facts. In order to decide what to do in the future we must at least "guess" what will happen, and consider the course of possible events with or without our interference in them. Even if rhetoric is applicable in both cases, it is necessary to distinguish them as two different forms of practical reasoning. Prudence, the rational custom of making decisions in a proper way, is the sort of virtue to be developed in both cases.

Another important theoretical clarification of the relation between legal and economic rationality, besides is the general character of the first and the limited character of the second. This has been disputed by "law and economics", as some authors try to include all normative reasoning in the realm of instrumental reasoning. Another school of thought that assumed that economics represented the most general field of knowledge in the human sciences is Marxism: Marx explicitly makes the point that what he calls "economy" is the whole realm of human activity, of which the exchange of goods is only a small part, even if it has a determinant influence on all others, as it is the one closest to the material reproduction of life. This was one important point in which he differed and diverged from the "classical" Ricardo. In spite of the long and deep discussion that such an assertion can inspire, I will assume there is this difference between law and economics exactly because in economic reasoning the result of one's action that is submitted to scrutiny or deliberation plays an important role and, as classical philosophy would say, the result of the action can be separated from the agent.

Morality, on the other hand, is usually one step away from instrumental reasoning. It is a matter of course that in deciding what to do, in deciding what is the right

thing to do from the moral point of view, results will play an important part. In a classical example in his discussion of how the statutes (positive law) should be applied, Aquinas says that the ultimate sense of every case has to be found in what is just, and what is just is a certain "state of affairs". Thus, if there is a certain time of the evening when the city gates are to be closed, in order to guarantee the safety of the city dwellers, or in his wording, with a view on the "common good", a resident who is trying to escape from a band of robbers has a right to have the city gates open for him even after hours. In his interpretation, the sense (purpose, end result) of the law that sets a time limit for the opening of the gate is to save lives, and it should not be interpreted in such a way as to needlessly let one city member die (cf. *Summa Theologiae* II, II ae, q. 57). He even cites Modestinus' phrase in the *Digest*: no reason should be strong enough as to interpret the laws in such a way that what was made to give men a good life should result in their own loss (*Nulla iuris ratio aut aequitatis benigna patitur ut quae salubriten pro utilitate hominum introductor, ea nos duriore interpretatione contra ipsorum commodum producamus ad severitatem, D. 1, 3, 25*). We can find a similar statement in John Rawls, when he is trying to clarify his differences with utilitarian reasoning. Rawls says that any ethical theory that does not take into consideration the results of actions is senseless.

Can legal rules be used to justify decisions over what to do in the future? Are cost-benefit arguments legal arguments? To answer this question I will try to give several examples drawn from the civil law tradition. We have reached a core issue in our course of reasoning. What sort of evidence, what sort of fact can be used to justify decisions?

2 Economic rationality in legal practice

In his important speech of presentation of the civil code draft, in 1804, Portalis made an interesting remark on the relations between law and other disciplines.

> "There are things about which justice is clear and manifest. A partner, for instance, is willing to share all the profits of the partnership without sharing the risks; the claim is outrageous; it is not necessary to inquire beyond the agreement itself for an iniquity created by the very letter of the agreement. But there are things in which the question of justice is complicated with other issues, alien to jurisprudence. Thus, it is in our acquired knowledge on agriculture that we should look for justice and injustice, usefulness or danger of certain clauses contained in given land lease agreements. It is our knowledge of trade that put an end to the endless disputes on the interests on loans, on monopolies, on the legitimacy of certain conditions within maritime contracts and so many other similar businesses. We can see that in these matters the legal question is subordinated to questions of calculation and administration."
> (Portalis 1999, 51)

From this point of view the adjudication of some matters depends clearly on "technical" knowledge and there is the possibility that the authority in charge of taking the decision will rely heavily on information – findings – provided by technical experts. This part of the process of decision-making is part of the fact-finding process with one important difference: the facts, which should be disclosed, are not facts of the past, but forecasts, possible scenarios.

With this in mind, we can approach the issues of distributive justice and the many cases in which law assumes that possible (foreseeable) results can be part of the foundations or justification of decisions.

2.1 Distributive justice

The traditional distinction says that distributive justice applies in the sharing of common goods or *status*, while commutative justice is related to exchange of goods. In contemporary or more familiar terms, distributive justice deals with the rules of non-zero-sum games, whereas commutative justice deals with zero-sum games. Before the XVIII Century, law and lawyers should be experts in both cases of justice, as both cases were considered to depend on *rules*.

In the course of the XVIII Century both the form of the State and the purpose of law went through important changes. The most interesting in terms of reasoning is the division between politics and law based on what one might see as the object of the dispute or conflict. There are two important cases in the history of the civil law tradition, cases that can be taken as examples of what happened in several countries: France and Prussia. By different means France and Prussia had to change their administrative machineries. In France, change came through the Revolution; in Prussia change came along the absolutism ilustrado. Legal scholars and state reformers clearly tried to separate political matters from legal matters. It is fairly well known that "courts" of the Old Regime would adjudicate matters of commutative justice (contracts) and retributive justice (crimes) as well as distributive justice (like the definition of prices of sugar in the city of Salvador, for the *Relação da Bahia*). The liberal or bourgeois state had to reshape the whole issue.

The first important step was a distinction between rights and interests. It is more than well known that during the XIX Century legal scholars debated the nature of rights (subjective rights) and finally called them "legally protected interests". This meant that there might be "unprotected interests", or simply interests. Rights were the object of law; interests were the object of politics. Law did not protect simple interests, so they could be altered, restricted, affected by legal change and government interference.

The itinerary of such separation can be traced back to the late XVIII century, but was made clear throughout the XIX century and even in the early XX century. Portalis, in his presentation of the Code Civil stated that "the ordinary contracts

between individuals" should not be confused with "commerce at large, whose function was to bring nations together and provide for the needs of the universal society of men" (Portalis 1999, 53). He was still insisting on a division that could be attributed to the affairs of the State in the Old Regime, that is, there should be some areas in which the general interest was to rule over private contracts.

The second important step was the separation of common or regular courts (judicial courts) from administrative courts. Apparently the only difference between both systems of "courts" is that administrative courts decide cases in which one of the parties is a governmental department, officer or agency. But when we look at the legal doctrine written on the subject it is clear that this is not the only issue at stake. It was recognized, for instance, that whenever the Administration was a party to a contract, ordinary courts could decide the case. So what was really at stake was the nature of the conflict: administrative courts would have jurisdiction when the case involved the "public interest". This was the XIX Century doctrine.

The idea of *public interest* covered the problems of "collective goods" or "commons". It also covered problems of general "welfare" in several senses. What in fact was at stake in the division of politics, law and administrative law was, in my opinion, the division between matters of commutative justice and matters of distributive justice. If the conflict was one that could be translated into the language of individual exchanges, it was a matter of law: torts, contracts, crimes were all matters in which justice meant a correction, a redress or an exchange. If the conflict was such that it could only be decided in terms of proportion or distribution among more than one party, or if it dealt with "indivisible goods", then it would be considered a matter of administrative courts, administrative law, and official discretion was acceptable in the settlement of the case. Regular judicial courts should not mediate, should not act with discretion: administrative courts and officers could, and should, decide cases by mediation and could pass judgments based on distributive aspects of the case.[3] France, Germany, Italy, Spain and Imperial Brazil, they all had their administrative courts system, where cases against the Administration should be decided.

So, by the end of the XIX Century and the beginning of the XX Century the matter was fairly well established, and legal scholars had abandoned the field of collective goods, collective interests or general welfare to the realm of politics, or to "administrative discretion". It seemed to be the realm of pure "convenience" rather than the field of rules and principles. Matters of interest were not matters of law. They would deal with "usefulness" or "prospective gains" of individuals, but they were not a matter of duty or obligation of the Administration, that is, they were not a matter of rights of individuals (Souza 1862, 90).[4]

There has been a considerable change in XX Century legal scholarship and it has been pressed to incorporate distributive disputes. In other words, legal scholarship

has been challenged to incorporate a theory of collective goods, a theory of proportional distribution of burdens and benefits and to incorporate a theory of purposive acts, actions and activities that had been basically exiled from legal reasoning. Legal doctrine had developed a fairly sophisticated account of collective goods. It can still be found in any civil code of the continental tradition under the name of "indivisible goods". The Brazilian civil code is just one of the countless examples: "Divisible goods are those that may be divided without change in their substance, or considerable decrease in their value, or uselessness for their intended use." (Art. 87) The wording of the civil code of 1916 was slightly different: "Divisible things are those that may be divided into material and different portions, each one forming a perfect whole" (art. 52). If one thing (or good) can be divided but will change its nature, the law may treat it as an indivisible thing; private parties can also treat things as indivisible wholes. Based on this latter idea, commercial lawyers developed the doctrine of the "azienda" ("estabelecimento", "Konzern"). This is a very useful device, but I would say that it had been practically abandoned as a general concept. This is why so many "rules" concerning these matters are usually not accepted as part of the "real" law.

Economists, however, have kept the idea alive and problems relating to "collective goods" and "collective actions" have played an important role in economic analysis.[5] Lawyers, instead, have concentrated in the idea of "public goods" with a totally different meaning. In fact, the civil code also mentions "public goods" or "public things": in Brazilian law public good means "state property" (federal, state or local). Public good here means the opposite of private property (Código Civil art. 98). So the name "public good" is used only to give an answer to the question: who owns this piece of real estate? Who owns these shares of the capital of this corporation? Who owns this street? If the answer is the state, then that will be considered a "public good".

This, however, is much more the result of the symbolic hegemony of commutative justice in legal reasoning than a fact within the legal system itself. It is fairly easy to find instances in which law has kept the reasoning of distribution. What will follow summarizes a few examples of the survival of distributive disputes in law. The socialist movement, the working class claims were probably the place where "distributive" matters and law met once again.

2.2 Economic law and regulation -a historical experiment from Vargas to Sarney (1930-1985)

Economic reasoning and law converged in the middle of the 20th century when welfare, development and planning gained a constitutional role from the times of the Mexican Constitution of 1917 and the Weimar Constitution of 1919. The constitutional discussion in Germany in the 1920s had precisely this issue in view. In

the case of Brazil, the 1934 Constitution gave the State a political (and legal) obligation of fostering development in order to structurally change the Brazilian society. Important legal experiences in this field were the so-called development programs. Beginning with the Juscelino Kubitschek Administration, different presidents presented Congress with development plans. Under the 1967 Constitution, development plans were incorporated into the pluriannual investment budget. A few legal scholars wrote on the subject at that time. They agreed that several of the most traditional concepts of legal scholarship would have to undergo some sort of change or specification.

Historically speaking the debate during the first years of the Vargas years involved two different schools of thought. In the one hand, *liberais*, such as Waldemar **Ferreira**, criticized the establishment of agencies (*autarquias funcionais*) that would assume both quasi-legislative and quasi-judicial powers. Ferreira was loyal to the Republican ideals of 1891: he believed that the separation of powers was a principal condition of freedom. In the opposite field were Francisco **Campos** and Oliveira **Vianna**, two leading figures of the regime. They were on the side of transforming labor committees, which existed in several states, into a federal system of administrative courts. *Justiça do trabalho* was first established as a department of the Executive branch (within the *Ministério do Trabalho*). Oliveira Vianna and Campos showed that among the powers of the *Justiça do Trabalho* were the settlement of disputes (individual or collective) by means of compromises. When a court did that, it was not actually adjudicating: it was mediating. That was one of the reasons to withdraw labor courts from the judicial branch at that time.

Campos and Vianna were also in favor of the establishment of autarquias (agencies) that would conduct the economic development. Partisans of Vargas were, at that time, drawing heavily on examples from the American experiment with agencies: they would cite not only agencies created by Roosevelt's New Deal. Of course, this was both a sincere belief that state intervention and liberal institutions were compatible, and an argumentative strategy, as the Republican Constitution of 1891 had been clearly a source of Americanization of Brazilian public law. If the Americans were doing that with their constitution in force, there was no not reason to keep the separation of powers and at the same time create new agencies. So there was some precedent on the discussion of law and economics in the Era Vargas.

The debate in the 1970s (the military regime) was a little bit different.[6] Agencies were an established reality. What was apparently new, or at least taken more seriously, was the idea of a global planning of the economy. Since the 1950s, the JK years, the *cepalinos* believed that a general view of the economy was essential. State decision should not be guided by partial action in different sectors. The

American experience was of much lesser help in these circumstances. Contrary to what had happened in Europe, Brazil and several other places, the USA had never established a constitutional welfare state. Welfare rights were not written in the constitution.[7] If the examples used by the Vargas regime were imported from the American tradition, during the military regime examples came from the post-war European states. The French tradition might be useful, and in fact that is what happened. When reading Brazilian legal doctrine concerning administrative law and financial law at that time one will soon discover that it was the French who were cited. The theoretical influence of the French administrative law was very important. The few legal scholars who dedicated themselves to the subject usually refer to French scholars and the fairly well established difference between the *effectiveness* of plans: plans were binding on the Administration (direct and indirect), but were only indicative to private corporations. Two separate fields of public law had to be joined to give some legal rationality to what was being done: *direito financeiro* and administrative law. A new classification of laws was made to accommodate what was then called *Massnahmegesetz, leis medidas, or leis de efeitos concretos*. But the import of the European model was not simple. There were important institutional differences. In the European tradition there were systems of administrative courts, ordinary judges were career judges, and Constitutional Courts had exclusive jurisdiction on constitutional matters. That is a totally different design from the Brazilian republican tradition, where career judges had powers of review and where no administrative courts existed. It was predictable that institutional conflicts might arise, as in fact, after the 1988 Constitution they appeared with growing importance and growing levels of reciprocal interference between the Executive and the Judicial branches.

It was accepted that plans, by their own nature, would cause differentiations. In this respect it would be acceptable that results of economic legislation would not affect every citizen equally. It was further agreed that economic legislation dealing with development and planning could be changed and revised without granting citizens, in principle, rights of compensation against the Administration (**Couto e Silva,** *RF* 278, 368). Statutes concerning economic legislation were considered naturally "flexible", that is, they would bind but within the limits of "economic possibility" (**Grau** 1978, 238, **Grau** sdp, 282). So, the tort doctrine had to be reviewed to accommodate state liability in the case of development policies or economic planning. Government action in these fields should not be strictly compared to breach of contract, breach of promise or traditional tort cases in general.

The doctrine of economic legislation and economic planning in Brazil has its own history of failure. Economic planning was identified with the military regime and with its final and long economic crisis. On the other hand the doctrine created along the economic planning issues at the federal constitutional level was never really

applied in other fields in which law met other disciplines, such as urban planning or environmental protection. The theoretical problems involved in economic planning were not always acknowledged as being of a similar nature of those in other fields in which statutes would refer to specific objectives and results.

Economic planning during the military regime shared the fate of budgetary legislation in general. In fact, development plans had to be translated into the language of budgetary provisions and were then given the name of "pluriannual investment budget". At that time, Congress had lost its power of amending the budget proposal, so it was fairly easy for the common sense of younger legal scholars and federal judges to assume that economic planning and dictatorship went hand in hand and the only way to defend democracy was to limit, as much as possible, the powers of the Executive power to interfere with economic planning.

Another aspect of the crisis of the 1980s was the growing rate of inflation. In trying to curb inflation, the Executive branch would from time to time take legislative initiatives (either through *decretos-leis* or later through *medidas provisórias*), which would normally be called "economic plans" or "stabilization plans". Most of these "plans" were short-lived and were not capable of putting an end to inflationary spirals. Courts and legal scholars were then caught in the middle of the crisis without being able to give adequate answers. The most important example was the reaction of the Supremo Tribunal Federal during the 1990 monetary reform program of the Collor Administration: it refused to decide the issue of the constitutionality of the stabilization program and did not take the risk of adjudicating such a serious matter with unpredictable consequences.

2.3 Private law and procedural law

It is not only the law of planning or economic law that provides interesting examples of the use of "economic" reasoning into law. I would like to give a few legal institutions of this nature in the most traditional fields, in private law and procedural law. One can find several instances of cost-benefit reasoning and forward-looking rules in private law. In several cases, private law will establish results to be attained, and parties and judges can and should consider these results to determine what is legal, illegal, just or unjust.

If liability is traditionally ascertained as a means of corrective (commutative or punitive) justice, does it apply equally to matters of economic regulation? If economic regulation is taken "caeteris paribus", if it is, by definition, dependent on contingent events, how do you adjudicate regulation? Is there a special liability in case of distributive justice? What is it? What sort of liability can be found in cases of plans and results to be achieved? Legal doctrine has a traditional example of dealing with the last issue, that of results to be achieve, but I am not sure that it has been sufficiently expolored in public law. I am referring to the classification of obligations into

obligations of means and obligations of results (obrigações de meios e obrigações de resultado). The distinction was created by Demogue, and widely used (**Pereira** 2002, 33, Gomes 1988, 451). Some civilists reject it as a general classification, but they acknowledge that it may be useful "to ascertain liabilities" (**Pereira** 2002, 34), or to determine the "ônus da prova", the "burden of the proof". In fact the difference between them lies in the extent to which the obligation has been performed and in case of nonperformance what sort of evidence would provide the debtor with a legal "acquittance". In case the obligation is one of "means", the debtor is considered to have complied with it as long as he has used "due diligence" to perform his duty even if he has not been able to produce a certain "result". If the result is what is actually due, the creditor has a right to compensation if the result was not finally produced. The debtor will not be held liable only if she shows evidence that the performance became impossible without her fault (as in the general cases). We are all familiar with the most traditional example: a surgeon is bound to perform a surgery with "due care" and using the best techniques he knows, etc, but he is not liable for the result of the surgery (the issue is put in a slightly different way in cases of esthetic or plastic surgeries for esthetical and non-functional purposes). Liability is just one case in which the forward-looking, distributive character of legal rules is to be reconsidered. Other examples may be found.

2.3.1 Corporations, contract law and procedural law

Corporations and partnerships are areas in which distributive rules play a central and constitutive role. Even if some civil codes define partnerships (*sociedades*) as bilateral contracts, many scholars have always insisted that partnerships should not be treated within the same framework as sales (*emptio venditio*). In partnerships there is what Ascarelli called a plurilateral relation (Ascarelli 1949), so that reciprocity is not commutative, but distributive and proportional among the partners. In partnerships the "contractual" relationship is of an on-going nature, it is made to last until it reaches a final purpose (the object of the partnership, the "*objeto social*"). The duties of the partners have to be evaluated from the point of view of their cooperation for the attainment of the common purpose. The social capital has to be treated as a common stock (community property) and until loss or profits are finally distributed individually at the end of each year or at the end of the partnership itself, each partner is not considered to have a "right" in any specific part of the common assets.

Cost-benefit analysis is imported into legal reasoning in civil procedure. Art. 620 of the Civil Procedure Code provides that the enforcement of decisions (*execução*) should be made at the least costly way as regards the debtor when that is possible. Another instance of cost-benefit analysis is the so-called principle of procedural economy: art. 244 of the CPC provides that procedural acts should not be invalidated when they have been functional to their ends, in spite of their form

(except when there is specific legal prohibition of it). The Criminal Procedural Code (CPP) provides another interesting example: art. 563 provides that no act shall be nullified unless it results in a "*prejuízo*" (loss) to either defense or accusation. These are all examples of the use of cost-benefit analysis in law. In all these examples the legal argument can incorporate a discussion of the results of the act, in spite of a previous definition of formal legality. The reasoning is based on results, not on principles.

2.3.2 Family law

One of the most typical cases of cost-benefit analysis can be found in family issues, particularly in alimony legal suits. Cases of alimony are the best-known example. In deciding a case of alimony there are several issues at stake. The first one is: is there a duty of A to pay alimonies to B? The question may be slightly complicated as the duty of A can coexist with the duty of C and D: suppose a father or mother who is ill and needs assistance. All of his or her children have a duty to assist them, even though this duty may be shared in different proportions. The second issue has to do with "how much". Courts have tended to define standards. It has been adopted as an acceptable measure that the debtor should pay one-third of his income to the creditor of alimony. This rule tends to be adopted to ordinary cases, when the debtor has a regular job, usually as an employee of a regular business corporation. Things get a lot fuzzier when courts deal with great fortunes or with people who do not earn regular salaries. In such cases empirical surveys might show that there are lots of compromises and family courts act more like mediators than adjudicators. A close analysis of these cases shows that judges, just like administrators, have a great deal of discretion in these cases. I would say that this discretion results from the very nature of the conflict before the court.

Cases of child custody are also a good example. A judge is allowed to give the custody to the parent (or adult) who is most likely to give the child better living conditions overall taking into account past events. In family law, therefore, cases of child custody may be decided on the best interest of the child. Consideration of potential results may enter the *ratio decidendi*. These cases have not been charged with the accusation of being non-legal matters.

2.3.4 Criminal law

This is also true in criminal law, to a certain extent. The criminal code provides for a certain "spectrum" within which the judge may apply the penalties to the convicted person. But in the course of his penalty, the law provides for possible reductions and changes. These are considered "disciplinary" or "administrative" matters, but some of them are decided by a judge (*juiz das execuções penais*) who supervises the application of the law.

These examples show how "judicial discretion" may be viewed as the equivalent, in terms of reasoning, of "administrative discretion".

2.3.5 Anti-trust law

In antitrust law, certain mergers may be acceptable and licit (legal) under the proviso that some results will obtain and that benefits shall be distributed through the "market". If the business corporations concerned show sufficient evidence that the overall result of their merging process will bring considerable benefits to consumers, they will be allowed to merge. The legal decision will explicitly incorporate future (probable) results as its basis (foundation, motivation, *ratio decidendi*).[8]

2.3.6 Res iudicata

In most, if not all the cases mentioned above, there is a legal exception of the *res iudicata* principle. It expressly admitted by art. 394 and 401 of the Cógigo Civil (cases of child custody and alimonies). If changes occur in the life conditions of creditor or debtor, the judge is allowed to change the rulings.

The *Class Action Act* (Lei da Ação Civil Pública, lei no. 7.347/85) created the so-called "civil inquiry", led by the Ministério Público. This has been the favorite locus for compromises, where the potential defendant may accept a "compromisso de ajustamento de conduta", where he negotiates the terms in which he will, in course of time, change his activity or behavior. Similar things can be found in the Anti-trust Act, in the case of the "compromisso de desempenho" (performance agreement) in art. 58. Even after a decision has been rendered, the administrative court will follow the activities of the interested parties to veriffy if results are or are not being achieved.

When reviewing the literature on economic planning the same characteristic may be found. When legal scholars say that plans can be reviewed and their foreseen results do not create any subjective right to individual citizens, they are probably dealing with something analogous to the alimony cases. Economic regulation is permanently subjection to changes in view of the results to be obtained. Now this, of course, should work in many directions, including the well-known "adequacy of the economic and financial balance of public contracts". In case of excessive gains – or excessive losses – the private operator of a public utility could be subject to re-discuss the terms of the agreement.

This basic idea has some complications when we deal with macro-economic themes. First, the fact-finding will show a particularly complex nature. Facts of the macro-economic level are not brute facts: many of these are institutional facts. The very word "market" is of this nature: there is the ideal market, an ideal-type used by economics to refer (I would not say describe) to the "reality" that needs to be built and needs to be "saved" or "maintained" by a system of collective action and collective intentionality. There is, on the other hand, an actual market. This actual market

is referred to in the anti-trust legislation as "the relevant" market. There is also a lay, ordinary language use of the word "market". How far does it identify with the use of the term in economic researches? How far is it co-extensive with the word used in a specific research? How far should this research go to define the market? Is "market" co-extensive with "society"? When the law says that the Agency should take into account the public interest, the national interest or the general interest, how does the actual "market" or even the "ideal" market fit into it? Now in adjudicating or deciding matters of regulation an authority has to refer to "the market" in at least both these senses.

Concluding remarks

A quick look at the statutes that created the new regulatory agencies in Brazil in the late l990s gives a meaningful insight into the theoretical problems that lawyers may face when interpreting and applying them. Two examples may suffice: Lei no. 9.472/97 (telecommunication industry – Agência Nacional de Telecomunicações) and Lei no. 9.478/97 (oil industry – Agência Nacional do Petróleo).

The law concerning the oil industries begins with a broad provision on the purposes of the national energy resources policies. Art. 1 states the purposes (objetivos) of the policies (in its caput). Some of them are rather general and open an immense field for discussions and interpretation: to secure the national interest, to promote development, enlarge the labor market, to protect the environment, etc. From any point of view they give rise to a variety of questions. Many of them – if not all of them – are potentially contradictory and they cannot be pursued all at the same time, except by distributing benefits and burdens in different proportions. It is basically impossible to foster capitalistic use of energy and save the environment, as it is very difficult reconcile captital investment and protection of the labor market. One possible solution for the simultaneous implementation of all these principles is to consider them under one very general policy to create an energy market in the country and then try to distribute the benefits of this market. So what is clearly the case is that these purposes can only be integrated in a distributive system, in which a zero-sum (exchange) rationality is not adequate.

Provisions of this sort were much less of a problem in a time when Congress passed, following the initiative of the Executive branch, the National Development Plans. In that case, Congress would set general economic policies, by means of the National Development Act, and specific numbers would be defined as results to be achieved. After the failed military regime and the change in the international financial and economic scene, confidence in National Development Planning dropped sharply and a political discussion, that could take place in a political sphere, is diverged to the regulatory agencies. Nowadays, the new agencies not always have an

integrated agenda of development, and the numbers that once were in the *planos nacionais* may be found in the concession agreements or in autonomous decisions of the agencies boards. Problems of interpretation of the agencies' rulings are then multiplied, as they will face problems of political (and constitutional) legitimacy. Should they be given complete freedom of action and should they be given complete freedom of action based on "technical expertise" alone? Problems of this nature have surfaced in the last months.

Another important aspect of of the law is that it incorporates into the legal world economic, political and social objectives. The Administration is charged with the task of creating things that do not necessarily exist and things that are not simply "things"; they are social conditions and can best be visualized as aggregate values. They are "states of affairs". The wording of the law is essentially written in the language of macro economic (labor market, consumers interest, free competition), social and political theory (development and national interest). These are not ordinary concepts, such as 'land', 'children', 'motor vehicle', or others that can be found in other legislation. They are not things that are there. They may also hide enormous difficulties in the distributive agenda of the federal government, especially in a society as divided (in terms of social classes and regional differences as Brazil). Regulation that apparently increases the numbers of cellular telephne users may affect diversely the level of indebtedness of consumers, and an accurate study of this sort is not always conducted by the new regulatory agencies.

Many of these provisions open the doors for rationality, which is not just legal rationality, in the modern individualistic sense of pure commutative relations. They allow for the use of "technical" reasoning, which puts two difficulties to a "regular" legal reasoning. This sort of reasoning, as the examples used above help to understand, not controlled by legal means alone: the legality or illegality of a given act or business depends on criteria defined within the realm of another discipline. Second, the legality or illegality of the behavior or policy is made dependent on results: if it proves an efficient policy to a given result it may be legal, if it proves inefficient it may be illegal. In other words, a "prudential" reasoning (prudential in the Kantian sense) makes its way into the law. But that makes the judgment dependent on results, which, by definition, are contingent (when not random).

What is law today? Does it still command, prohibit and allow? Is it a change in law, a change in sources, and a change in the purpose of the political authority? For many, legal reasoning has been constrained to deal with qualifying behaviors as licit and illicit. In this respect, legality has been cut from any other consideration regarding the consequences of behaviors. From this point of view all decisions allowed to deal with the intended consequences of human action are assigned to different fields: politics, economics, ethics. This is not totally true: there are fields in which considerations of the utility and result of human actions are still allowed to count for legal purposes.

But law, also incorporates certain ideas that may be called absolute. Of course, one would be tempted to say that this is so only in contemporary Western philosophy, most notably in the tradition of natural lawyers. In fact, whereas it was hard to find any assertion that rights were absolute in earlier philosophers and lawyers, from the XVII century on lawyers begin to talk about absolute rights. Absolute rights have been translated into contemporary theories under the name of "non reciprocal" rights or relations. The holder of a natural, fundamental, absolute or 'non reciprocal' right enjoys the protection of the law no matter what he or she does to his fellow human beings. This idea of right is, of course, hard to combine with the relativism of economic thinking.

All this is law, and all this is legal reasoning. This is not considered typical in a perfunctory view, and some people would even ignore this as an important aspect of law. But that is only *per caso*. In fact, cases like these are not infrequent and legal professionals (scholars and practitioners) deal with them on a day-to-day basis. I would like to bring to light this fact to conclude that some of the changes through which nation-states, liberal states and modern contemporary states are going through may be, partly and only from the legal point of view, a rearrangement of functions that will make decisions, that is legal decisions, more like cases of family or antitrust. In other words, certain forms of legal reasoning that have been considered peripheral or secondary in legal thinking will probably become more important.

NOTES

1 The best comment on Kelsen's theory in the last years hás been Nino's explanation of the role of the *Grundnorm* in validity. (Nino 2003)

2 The famous study of Banfield (*The moral basis of a backward society*) might be a typical example. Traditional communities do not create separate spheres and then seem "disfunctional" to a modern eye.

3 Literature on the subject is growing. For the German case see in general Stolleis (1992), for the Italian case Grossi (2000).

4 Lon Fuller in his famous essay no the limits of adjudication does not mention this essential idea. This puts him into great difficulty as he tends to equate adjudication with commutative conflicts and commutative justice with rationality. Arguments of distributive justice, as in the tradition I am discussing here, are left to the field of political will, not arguable in rational terms.

5 Joseph Roemer asserts that "many economists who work in the areas of social choice theory and welfare

economics are quite unfamiliar with contemporary philosophical thinking on distributive justice" (Roemer 1996, 1) This is also true, I believe, of lawyers. As Roemer puts it, there has been a renaissance of philosophical interest in the matter since the publication of Rawl's *A Theory of Justice*. Thomas Wilhelmsson also shows how consumer protection has to be understood primarily from the point of view of distributive justice (or social justice, as it has been called by many in the XX Century due to the influence of Christian social thought).

6 A general overview of the historical development of plans in Brazil can be found in Bercovici, 2003.

7 The so-called "second bill of rights" is compatible with constitutional law, but is no written text (cf. Sunstein, After the rights revolution).

8 The Anti-trust authority in Brazil (CADE – Conselho Administrativo de Defesa Econômica) is probably the only existing example of na administrative court in Brazil. This is probably why the debates around its standing as an independent department is so strong.

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José Reinaldo de Lima Lopes

Professor Associado, Livre-docente
Faculdade de Direito da Universidade de São Paulo
Escola de Direito de São Paulo – Fundação Getúlio Vargas

INSTITUTIONAL DESIGN, NORMATIVE POLITICAL THEORY AND ACCOUNTABILITY

Marcus André Melo

INTRODUCTION

This paper is concerned with the link between institutional design and accountability, with a focus on the normative assumptions of current views about this link. The main question it addresses has to do with the effects of institutional design – or perhaps more appropriately, constitutional design – on several dimensions that are crucial for the ability of citizens to hold governments accountable. Accountability refers to both citizens preferences and to the rule of law. In modern democracies elections are the means through which citizens express their preferences. This has been discussed in terms of democratic accountability or 'vertical accountability'. Accountability is defined here as the capacity of citizens to sanction rulers that deviate from their electoral promises or more generally from the preferences of citizens. In this sense accountability is more than responsiveness: it implies the capacity to reward or punish and not only the capacity to listen to (Manin, Przeworski and Stokes 1999).

This is not all that there is to accountability. Accountability has also to do with citizen's control (or lack of it) over governments and over the behavior of public officials while in office. This involves the issue of the rule of law. Current discussions of institutional design and accountability have a number of frequently unspoken normative assumptions. One of the most important of these assumptions is a normative commitment to a majoritarian vision of democracy. This view is arguably the predominant view in most current discussions in comparative politics. In this paper, I discuss what Powell (2000) has called majoritarian design systems and explore its basic features and normative ideals. I then explore further its implications for a discussion

of accountability and of the efficiency of political systems. Although the focus is on political accountability and how it is shaped in crucial ways by institutional design, other broader determinants of accountability and of the quality of democratic governance are also considered.

Institutional Design and Normative Political Theory

Comparative empirical work on the functioning of democratic systems has led to a number of findings on the effects of institutional design on democratic governance. Although presented as value free empirical findings, part of this literature is usually very normative in its assumptions. But not only are these not made explicit or even recognized, its conclusions also remain to a large extent un-theorized. This might reflect the increasing division of labor between democratic theorists and empirically oriented researchers, but it is particularly true of the scholarship on the so-called new democracies. Democracies are evaluated in terms of their political efficiency in producing tangible results for the population but also in terms of their capacity to aggregate interests and produce authoritative binding decisions. The conclusions are typically that they do not in virtue of the persistence of clientelism and the like, but flaws in their overall constitutional arrangement has been persistently been detected.

The recent new wave of research in comparative politics has been influenced by the neoinstitutionalist approach. Tsebelis's analysis of veto players became the starting point for much of this strand of the literature. Tsebelis's contribution is primarily concerned with positive analysis and is concerned with explaining patterns of legislative output and the institutional determinants of policy stability and change. Undeniably, formal analyses of veto players contributed significantly to the understanding of the ways through which institutional variables affect the ability of governments to approve legislation and generated important predictions. The contributions in Haggard and McCubbins (2001) has explored the issue further and applied the related notion of veto gates to a number of policy areas, opening the ground for a many sectoral studies. While this line of analysis is primarily positive, many scholars who pursued it, and applied it in case studies, are not.

It is not frequently for scholars to make explicit their normative commitments. Stepan is one of the exceptions. In his comparative work on federalism[1] he is very critical of the functioning of several federal systems because they are "demos-constraining" (Stepan 2001). The author uses an index of representational inequality to measure this and is highly critical of the allocation of policy-making powers to subnational governments is also critically evaluated. While this kind of theorizing is at odds with current debates in democratic theory, it signals pretty much the tone of the existing scholarship.

The recent scholarship on Latin American political systems has emphasized a number of features that undermine the process of government formation. As a consequence of these features many countries in the region have difficulties in forming stable legislative majorities and are incapable of implementing mandates (Geddes 2003). Brazil is depicted in this literature as an extreme case of a fragmented polity. According to Ames (2002), for example, Brazil is a deadlocked democracy. A fragmented party system produces shifting and weak governing coalitions, which come into being after elections. These are unable to ensure a stable and predictable basis support for the Executive. Balkanization therefore ensues because individual legislators demand pork in exchange for support. Moreover, it is argued that as a result governments lack clear mandates, and consequently are non-accountable. Flaws in institutional design causes in low accountability. This is viewed as ultimately produced by a combination of institutional features, including open list proportional representation, federalism, presidentialism, judicial review, etc. As discussed in the remaining of the text, these features are crucial for a proportional vision of democracy and are not easily accommodated within the majoritarian design that many analysts seem to favor or more probably assume without recognizing.

Evaluations of alleged political inefficiencies or institutional flaws are sometimes based in concepts and instruments that are rooted in normative assumptions that frequently are not consistent with the general constitutional design of the countries. These evaluations inform demands for political reform, which are entirely inconsistent. The normative conclusions from these proposals as well as from the strand of the literature mentioned above are rooted in a majoritarian vision of democratic governance. Because it is assumed that the latter is the only possible alternative, these analyses and proposals are misleading in many ways.

Majoritarian and Proportional Models: normative assumptions

The contrast between majoritarian and proportional visions is an old topic in political science. Many of the early discussions on proportional representation illustrate the point. In current discussions of multiculturalism there is a renewed debate on the relative advantages and disadvantages of majoritarianism as a normative principle. The multicultural critique of majoritarianism builds on the century long criticism that it fails to account for the diversity of values in society, and articulates new issues such as identity, recognition and group rights. Because the focus of the discussion in this paper is on the links between institutional design and accountability many important aspects of the majoritarian versus proportional debate fall out of the scope of the discussion.

Lijphart pioneering contribution explored in detail the institutional features of the Westminster or majoritarian model and what he calls consociational or consensus democracies. (Lijphart 1984)[2]. Majoritarianism as *rule by a majority* embodies the

fundamental democratic principle, one that help us distinguishing democracies from authoritarian regimes. Needless to say that this is also shared by the proportional, or consensus vision. The distinction is that in the latter, it is the preferences of the largest number of people that should prevail. Governments should be responsive to not a majority but to "as many people as possible"(Lijphart 1984, 4). The requisite for a majority is viewed as a minimum prerequisite. The consensus vision is that institutional rules should enhance participation and enlarge the size of the majorities. By contrast, the majoritarian vision aims at ensuring that the preferences of the minimum majority are expressed in the democratic process. Here majoritarianism describes a vision and not merely the predominant electoral rule or the basic democratic principle that a majority should rule. Even in the restricted electoral sense, as Shugart (2001, 30) points out, the term majoritarianism is ambiguous: "The implicit assumption behind the term is that the system represents a majority of voters, although all the model of majoritarian governance requires is that a majority of parliamentary seats is sufficient to rule. Indeed single party parliamentary majorities are typically based on mere pluralities of the electorate, often in the range of 38%-45%."

Powell (2000) uses a similar terminology in his analysis of majoritarian and proportional designs but he is particularly concerned with the normative distinctions between the two and how it is reflected in electoral accountability – a point that is the focus of this paper. In the majoritarian (or power concentration) vision of democracy, the objects of citizen's electoral behavior are the office-holders which exercise concentrated policy-making powers. In this vision, power concentration is a pre-requisite for the adequate exercise of control by citizens through elections. This is so because power concentration allows clarity of responsibility. Conversely, power dispersion implies that policy making is the result of post –electoral bargaining within the winning coalition and with other relevant institutional actors and this would make it difficult to pinpoint retrospective responsibility to decisions. This view is associated with the idea of democratic *control* (as opposed to *influence*) by citizens and to a mandate notion of representation. Citizens exercise control by approving the policy proposals that are presented by would be officeholders in the electoral process. During elections officeholders are given a mandate to implement these preferences. The mechanisms informing citizens' choice are twofold and it is difficult to establish which one is at work. In one argument, citizens vote on the basis of the incumbent's past performances. Citizens punish or reward incumbents looking backwards and using a 'retrospective vote'. In a different argument, people exercise control in virtue of their ability to select prospective officeholders. In both accounts, concentrated power is necessary for citizens to control public officials and their use of the mandates vested on them.

The proportional vision offers a very distinct perspective on the democratic process. Power dispersion is viewed as a pre-condition for the effective representation

of the diverse societal interests. The basic objective is to enhance the influence of citizens on governments. Because power is dispersed, representation takes on the form of authorized representation to advance citizen's interests in decision-making. Unlike the majoritarian vision, citizens do not reward or punish officeholders, rather they elect them expecting that they act in the citizen's best interest. Representatives are viewed as agents or delegates of citizens. They are agents who the citizens believe will act as she or he would have acted if bargaining for him or herself (Pitkin 1967; Manin, Przeworski and Stokes 1999). The dispersed power vision assumes that citizens have heterogeneous preferences and that the democratic ideal is best encapsulated when this is reflected in the policy-making process.

A number of further distinctions can be drawn between majoritarian and proportion views. First, the disperse power vision confers important roles for the minorities. By assigning a role for the opposition in the process of governing, it is expected that the interests of all citizens and not only the interests of a single majority prevail. Second, in the power dispersion view some amount of discretion is implicit vested in the officeholders. By contrast, majoritarians aim to maximize citizen's control over elected representatives and to ensure that they are accountable to citizens. Two distinct views of representation underlie both visions. The power concentration vision assumes an "accountability view" of representation, as Pitkin calls it (1967, 55), in which no independent or autonomous judgment is expected of representatives.[3] In the proportional vision, office holders are delegates, which are expected to influence policy-making. The notion of accountability informing the earlier majoritarian visions tended to assume that the collective interests of the citizens existed and were identifiable. In addition the questions relative to the aggregation of individual preferences in a social welfare function (the existence of multiple single issue majorities, etc.) were left undiscussed. What seems to be implicit in many current discussions of institutional design and accountability in the comparative politics literature is that citizens confronted with policy proposals express their preferences and sanction or reward incumbents, and no explicit normative assumption is made about collective interests. Democracy is viewed in this connection as a competitive schumpeterian mechanism through which political elites get the approval (or not) of citizens for policy proposals that they formulate. The accountability view in this Rikerian sense does not require a notion of collective interest.

As Powell (2000) argues, for elections to serve as instruments of democracy, it is necessary that the incentives of backward and forward mechanisms (retrospective vote and selecting types) used by citizens are internalized by officeholders and become effective. In other words, it is expected that office-holders anticipating the possibility of rejection, adjust their behavior to citizen's preferences. Social choice theorists have highlighted the problems arising from identifying the package of policies that would reflect citizens's preferences. Whatever the congruence between

citizens's preferences and this package, the process originates in political elites mobilizing the electorates around policy proposals. Essential to this process is the mediating role of political parties which help citizen's selecting types – i.e. by grouping them into a political label.

When selecting would be policy-makers people confer an electoral mandate on the basis of the expected outcomes. On the other hand when selecting incumbents citizens get policy makers to account for decisions. But as Powell (2000, 11-12) argues in other to reject incumbents all that citizens need to know is who was responsible for actual outcomes. This has to do with the clarity of responsibility. Two preconditions are necessary for the majoritarian vision to be implemented effectively. First, citizens need to be able to identify future governments at the time of elections. If they do not expect that their vote influence the formation of governments, they have no incentive to vote strategically to shape future policy -making. Second, it is necessary that the winning electoral party or coalition form the government and implement the policy alternatives presented at the time of elections. If the institutional rules of a country make it necessary for the winning party to engage in post-electoral bargaining, or to interact with other institutional actors wielding veto powers, the impact of the voter's behavior is severely weakened.

While accountability and mandates are crucial for the majoritarian model, the assurance that the diverse citizens's interests are represented in policy-making is key to the proportional vision. Here accountability and mandates play no role; in fact they do not make sense because what is at stake is the representational congruence between societal groups or parties and policy-making powers. Proportional representation makes possible for the government to reflect in policy-making the existence of multiple majorities, varying according to issue area.

Constitutional choices and models of democracy

The visions of democracy discussed in the preceding sections informed the constitutional design of current democracies in ways which are not frequently recognized or even understood. Many analysts use the parameters that are appropriate for evaluating one of the models or visions to evaluate both. This is at the basis of the misleading criticisms of current democracies.

Two types of constitutional rules are crucial for understanding the vision of democracy underlying a country's political system. These are the representation rules and the rules governing the policy-making process. Electoral rules are key to determining the extent to which legislative majorities can be formed – an integral part of the majoritarian vision. Conversely, they can produce a dispersal of power and allow the representation of multiple parties, as required by the proportional vision. The constitutional rules can also produce dispersal or concentration of policy-making

powers. For Lijphart (1984; 1999) countries with majoritarian constitutional designs there is concentration of policy-making power and rules encouraging the formation of legislative majorities. Despite their enormous variation, electoral rules can be grouped in two types: single member plurality rule and multi member proportional representational. As discussed in the vast literature on the subject, these rules are strong predictors of the number of effective parties and of the electoral threshold (the share of vote needed to acquire representation). The empirical analyses of existing democracies have showed that as a rule legislative majorities are manufactured by the electoral systems. Single party vote majorities are very rare and single party pluralities is the common fact of political life.

A crucial constitutional choice bearing on electoral rules has to do with the trade off between inclusiveness and governability.[4] Inclusive electoral rules such as multi member proportional representation, low district magnitude and low electoral thresholds permits a wider representation of interests and foster multipartism. In turn, this enhanced participation tends to imply *ceteris paribus* more political transaction costs. Majoritarian design systems are those that opt for less inclusiveness and more governability.

Constitutional design implies a tradeoff between polities that offer choices of *governments* before elections and those that offer choices of *parties* after elections (Shugart 2001, 29). This tradeoff is between identifiability and clarity of responsibility, on the one hand, and representativeness, on the oter. As Shugart argues:

> "with representativeness maximized, voters are presented with a wide range of parties on several salient issues dimensions, but the probability that governments will be formed only after post-election bargaining means that voters are apt to have difficulty identifying the likely governmental options at election time" (Shugart 2001, 29-30)

Majoritarian design systems offers more pre-election identifiability, that is provide voters with clear choices of competing governments prior to elections.[5] As discussed earlier, this is one of the preconditions of the majoritarian model view of accountability. This produces clarity of responsibility and therefore citizens are better positioned to reward and punish officeholders. But this comes at a great cost. Pure majoritarian systems – which Shugart (2001) calls *pluralitarian* polities -face a *democratic deficit* that is produced by the fact that the majorities are only pluralities of the electorates. They are also prone to the problem of the "wrong winner" that occurs when the electoral rules manufacture a parliamentary winner that did not command a majority of the votes.

The rules governing the policy-making process has to do with the degree to which policy-making power is distributed between the Executive, the Legislative and the Judicial branches (horizontal separation of powers), between levels of government

(vertical separation of powers), as well as within the Legislature. Political systems of a majoritaian design typically have rules that encourage a single parliamentary majority to control policy making, have unified governments (parliamentary systems), are unitary and do not have judicial review. Within the legislature little or no power is given to the opposition and the legislative committees are weak. In addition, governments control the legislative agenda and the rules limits committee's amendment. [6]

By contrast, proportional design systems provide decentralized legislatures and or bicameralism, strong committee systems, and a role for the opposition (which controls committee chairs, etc). It is also associated with decentralized governments and federalism. Judicial review plays a key role in the majoritarian vision. Concertation mechanisms of interest intermediation and corporatist structures also characterize proportional designs. These concertation mechanisms may include societal interests as well as institutional actors such as governors or mayors.

In addition to the above, other anti-majoritarian institutions include constitutions, independent regulatory institutions and independent central banks. The mechanisms that ensure constitutional inertia include *inter alia* supermajority requirements for amendments, delays (proposed in one legislature, an amendment is voted in a subsequent legislature), ratification (by referenda or state assembly). The requirement for supermajorities is one of the most explicit features in proportional design systems. [7]

These antimajoritarian institutions like independent regulatory bodies challenge the prevailing view of accountability based on a majoritarian vision. This is so because the notion of a mandate is not applicable here. Independent regulators are closer to the idea of delegates who are expected to act in the interests of citizens. Mandates do not make sense in a context of incomplete and asymmetrical information between citizens (or politicians) and regulators. [8] Procedural and indirect control is the alternative (McCubbins and Schwartz 1984).

These features in fact represent veto players or veto gates. Because the number of players is larger, the level of *deciseveness* (ability to make decisions) and *resoluteness* (ability to stick to a decision when it is made) – of a polity is weakened. This is the trust of the argument of Cox and McCubbins:

> "Polities that combine institutional divisions of decision-making authority with political divisions of purpose will tend to be either indecisive or prone to morselizing public policy, or both. Institutional divisions of power can come in the form of presidentialism, bicameralism, federalism, provisions for judicial review, and so on. Political divisions of purpose can stem both from the inherent diversity of opinion within a nation's society and from the incentives that the electoral system presents to combine those diverse interests into many or few political organizations. Some electoral systems encourage the formation of a few hierarchical parties whose leaders internalize the

costs and benefits of public policy as it affects a wide range of the population. Other electoral systems facilitate either large numbers of parties or decentralized (factionalized or atomized) parties" (Cox and McCubbins 2001, 46).

VETO POINTS OR DELIBERATION?

While veto players analysis has important positive predictions, it fails to draw adequate normative lessons from it. The implicit normative vision in many of these analyses is that the fewer the veto points, the better the functioning of the democratic process. The problem is even more apparent in the discussion of accountability.

I wonder what would be the conclusions of many of these comparative scholars of new democracies to the fact that "in Germany the government succeeds in getting about 85 percent its initiated legislation passed by the bundestag, but it is very often that amended and altered in many ways to reflect a variety of specialized interests" (Powell 2000, 63).

Are the committee's to be interpreted as veto points or as mechanisms that ensure that policies represent the median voter?

Many veto points are viewed in a proportional vision of democracy as part and parcel of the institutional mix of an ideal polity. Take it for example the institutions associated with federalism such as the symmetrical bicameralism discussed by Lijphart (1984). In the absence of these institutions in large or ethnically segmented countries, the quality of democratic life would arguable deteriorate. The same applies to judicial institutions.

For the majoritarian vision, the democratic ideal is realized in the ability to reach decisions, implement them and get them evaluated at elections. This is tantamount to the idea of institutional efficiency as found in economic reasoning. Many of the institutional features of proportional systems are designed to encourage consensus by the largest number of parties. The deliberative element, which is a constitutive part of the proportional vision, is therefore devalued in the majoritarian ideal. This is best exemplified in principal-agent models in which the primary concern is the reduction of the agency losses resulting from the delegation of from citizens to representatives. However, majoritarianism seems to fail in its own terms (Powell 2000), and seems to be a manufactured creature by a number of institutional arrangements, particularly of electoral rules. It may also face problems of legitimacy, as exemplified by the UK.

While the dispersal of power view has to come to terms with the problems associated with governmental paralysis and stalemate that may occur in hyper-representative systems (Shugart 2001), comparative scholars have to face the many problem facing the majoritarian view discussed above. The language of institutional

efficiency that underlies much of their empirical work leads them to draw unwarranted normative conclusions.

NOTES

1 The author compares the US, Brazil, Mexico, India and Germany.

2 Dahl (1956) refers to "populist" and "Madisonian" democracy, and Riker (1982) to "populist" and "liberal" democracies. Powell (2000) talks about majority control versus proportional influence models or visions, and I will stick to this usage throughout the paper.

3 For Pitkin (1967), "the accountability view is a practical or empirical hypothesis disguised as a conceptual view "(p. 58). Putting forward the view that representation is acting substantively in the interest of the represented, she argues that the "accountability view does not tell us anything about what goes on during representation, how a representative ought to act or what he is expected to do, how to tell whether he has represented well or badly". (p. 58)

Elsewhere she elaborates this criticism further, as follows: "Accountability theorists are even more vulnerable in this respect [how to judge a representative performance]. Their aim is to show that true representation entails responsiveness to the represented, attention to his wishes or needs. And they see accountability as essential for achieving this purpose, hence as the essence of representation. Yet by defining representation in terms of accountability they defeat their own aims. By defining a representative as anyone who will eventually have to account to another for his actions, they make it impossible for the idea of representation to serve as a guide or standard for his actions. His conduct remains irrelevant to representation"(Pitkin 1967, 113).

4 A pioneering statement of this tradeoff is Dahl (1971), chapter 7.

5 For the discussion in this section I draw on Powell (2000).

6 See Powell (2000), Lijphart (1999), Strom (1990) and Doering (1995). Strom created an additive scale of 'opposition influence' in the legislature that has been used widely in the empirical literature.

7 In some countries like Brazil, however, the Constitution has become a source of rigidity not only for institutional matters, rights and procedures but also for public policy issues. The Brazilian Constitution of 1988 represented a foundational moment with important path dependent developments. Because it was a unique historical juncture, it incorporated a vast array of political, social and corporatist demands. As a result, with 250 articles in the main text and additional 75 provisional articles, the constitution is unusually long and covers many very specific non-constitutional issues of policy. The choice of creating such a wide-ranging and detailed Constitution could also be attributed to the lack of trust and credibility on politics at that time. Thus, to write an article within the Constitution meant a 'safe' institutional terrain in which political players could develop their political transactions with a minimal of certainty that their arrangements and agreements would be enforced. Consequently, the Constitution hard-wired many public policy issues by requiring constitutional amendments in order to change policy. It is highly significant that many subsequent reforms has implied de-constitutionalizing issues, i.e. deleting articles from the constitution and subsequently (but not always), legislating about the issue through ordinary laws. The initial high level of constitutionalization of public policy produced great rigidity in public policy in general. The preceding helps explain why the Constitution of 1988 is the most amended constitution in the country's history. Brazil's first constitution, passed in 1824 lasted 65 years and was amended once, whereas Brazil's second constitution which established the republican form of government lasted from 1891 to 1930 and again was amended only once. The constitution of 1946 lasted 21 years and was amended 27 times. The military constitutions of 1967 and 1969 were amended 26 times in a period of 21 years. By contrast, within 12 years the

constitution of 1988 has already been amended 37 times. Between 1988 and 2001 (February), 2424 constitutional amendments had been presented to Congress. Under President Lula da Silva, three new constitutional amendments have been passed. The yearly average amendment rate for the Constitution of 1988 up to the end of 2003 has reached 3.5. For the period 1992 (when the first amendment was approved) to 2003, the average rate of amendment is 4.4 – an extremely high rate by any standard. In addition to the procedural difficulties, it should be noted that constitutionalization and deconstitutionalization (i.e. inserting and deleting provisions from the constitution) are very distinct and asymmetrical political processes. For consitutionalization, collective action problems undermine the ability of public to insert particularistic interests. For de-constitutionalization the opposite holds; withdrawing benefits and rent seeking privileges from the constitution requires overcoming the resistance of organized and sectoral interests. Reforms that de-constitutionalize issues generally lead to legislation on the issue or issuing *medida provisória*. In this game a lack of trust and the opportunity for opportunistic behavior has precluded some welfare enhancing deals to take place. The lack of trust arose because the executive holds great agenda powers and decree authorities. Many members of Congress saw the deletion of articles from the constitution as a mechanism for the executive to unilaterally impose its preferences. In other words de-constitutionalizing is seen by some as equivalent to giving a blank check to the executive.

8 See Levy and Spiller (1996). See also Shapiro (1997) and Majone (1999)

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Marcus André Melo

Professor of Political Science at
Pernambuco Federal University

THE CHALLENGE OF POOR GOVERNANCE AND CORRUPTION

Susan Rose-Ackerman [1]

All political systems need to mediate the relationship between private wealth and public power. Those that fail risk a dysfunctional government captured by wealthy interests. Corruption is one symptom of such failure with private willingness-to-pay trumping public goals. Private individuals and business firms pay to get routine services and to get to the head of the bureaucratic queue. They pay to limit their taxes, avoid costly regulations, obtain contracts at inflated prices, and get concessions and privatized firms at low prices. If corruption is endemic, public officials, both bureaucrats and elected officials, may redesign programs and propose public projects with few public benefits and many opportunities for private profit. Of course, corruption, in the sense of bribes, payoffs and kickbacks, is only one type of government failure. Efforts to promote "good governance" must be broader than anti-corruption campaigns. Governments may be honest but inefficient because no one has an incentive to work productively, and narrow elites may capture the state and exert excess influence on policy. Bribery might induce the lazy to work hard and permit those not in the inner circle of cronies to obtain benefits. However, even in such cases, corruption cannot be confined to "functional" areas. It will be a temptation whenever private benefits are positive. It may be a reasonable response to a harsh reality, but, over time, it can facilitate a spiral into an even worse situation.

"Corruption" is a term whose meaning shifts with the speaker. It can describe the corruption of the young from watching violence on television or refer to political decisions that provide narrow benefits to one's constituents in the form, say, of a new road through the district. In short, speakers use the term to cover a range of

actions that they find undesirable. Because my topic includes both corruption and poor governance, I omit both morally corrupting activities, on the one hand, and run-of-the-mill constituency-based politics, on the other. I use the common definition of corruption as the "misuse of public power for private or political gain," recognizing that "misuse" must be defined in terms of some standard. Many corrupt activities under this definition are illegal in most countries—for example, paying and receiving bribes, fraud, embezzlement, self-dealing, conflicts of interest, and providing a quid pro quo in return for campaign gifts. However, part of the policy debate turns on where to draw the legal line and how to control borderline phenomena, such as conflicts of interest, which many political systems fail to regulate. As I outline below, one of the most important debates turns on the issue of "state capture" or the problem of creating open democratic/market societies in states where a narrow elite has a disproportionate influence on state policy. In those countries outright bribery may be low, but the system is riddled with special interest deals that favor the few over the many.

Researchers at the World Bank estimate that worldwide bribery totals at least $1 trillion per year, just over 3% of world income in 2002. The Bank staff extrapolated from firm-and household level data contained in their own country-level surveys so the number represents an order of magnitude with a large margin of error.[2] It is an estimate of the volume of bribes, not the impact of corruption on economic growth and global income. If used to measure the costs of corruption, it assumes that the volume of payoffs is a good proxy for their economic effects. This, of course, need not be true. In economic terms bribes are transfers from one pocket to another and are not an accurate measure of corruption's impact. Rather, the economic costs are the distortions induced by these transfers. Those costs might be many orders of magnitude higher than the volume of bribes themselves, or they might, under some conditions, be lower. Bribes might be small in some countries because bribe payers have bargaining power and do not need to pay much to get large benefits. In other countries, public officials may be able to extort large payoffs that represent most of the benefits of the corrupt transaction. The estimate also ignores the role of corruption in increasing inequality and undermining support for democracy. Nevertheless, it provides a starting point from which to develop more fine-grained estimates.

Pointing to the magnitude of the problem, however, does not determine solutions. Because of the diversity of circumstances that produce corruption and poor governance, it is difficult to propose global approaches. Nevertheless, in what follows I make an effort, recognizing that improving governance in individual countries will require carefully tailored policies carried out with the hard work and personal commitment of those on the ground. Estimates of costs and benefits are obviously only rough guesses. However, it is important not to overlook reform possibilities in this area. Some reforms, if well designed and implemented, would have large benefits and

very low costs. Unfortunately, they also have serious distributive effects, and those who gain from the status quo are frequently powerful economic and political actors capable of blocking reforms.

Cost-benefit ratios for other types of reforms will be distorted if they do not take corruption, self-dealing, and incompetence into account. Thus, the risks of corruption and weak administration need to be considered in assessing proposals, for example, to limit hunger, reduce violence, or improve education and health.

The options that I discuss fall into five categories: voice and accountability, procurement, revenue raising, regulation of business, and international efforts to limit high-level corruption in international business.

First, I summarize many successful examples of programs that improve accountability at the grass roots and argue that these cases provide lessons that can be applied elsewhere. Some cases, such as school financing in Uganda and public works construction in Nepal, suggest that relatively simple, inexpensive reforms can have large benefits if the political will exists.

Second, I recommend efforts to develop benchmark cost estimates that can help constrain procurement fraud and corruption. This would require coordinated data gathering efforts, but the giving the large cost distortions in contracting, sometimes up to 30-40%, the gains could be large. Under some conditions, a state could combine benchmarking and citizen control to constrain waste and malfeasance.

Third, I consider reform of revenue collection through tax simplification and incentive-based reforms. Once again the net benefits of a well-designed program can be large, but the mixed record of past efforts suggests caution.

Fourth, I recommend the streamlining of business regulations based on data indicating the economic costs of "red tape." However, past work has only looked at the gains to business and had failed to consider the costs to society of eliminating regulations that provide social benefits. Thus policy must balance benefits and costs of regulations.

Finally, I discuss international initiatives to increase transparency in international concession contracts for natural resources and efforts to track down the assets of corrupt officials. The former option is also recommended in Paul Collier and Anke Hoeffler's (2004) paper on civil war for the Copenhagen Consensus. They estimate that it could provide multi-billion dollar benefits with minimal costs. Like the other options on my list, however, there is a dearth of actual experience with putting this idea into practice. One should follow an experimental approach to see what works and what does not.

This paper focuses on empirical evidence. It does not discuss theoretical work on the causes and consequences of corruption and poor governance. Those who want to pursue these issues further should consult my two books—Rose-Ackerman (1978) and (1999), a review article by Pranab Bardhan (1997), and the framework presented in Shleifer and Vishny (1993). These sources also include extensive references to

the literature. To access current work, the World Bank Institute maintains a website [http://www.worldbank.org/wbi/governance] as does Transparency International (TI), an international nongovernmental organization committed to fighting corruption [http://www.transparency.org]. Several recent literature reviews are at the website of U4 Utstein Anti-Corruption Resource Centre at http://www.u4.no.

I. Research on the Causes and Consequences of Corruption

Several strands of literature demonstrate the benefits of corruption control and government reform. I begin with cross-country studies that try to explain the consequences of corruption and poor governance for economic growth and well being. The next section considers firm level surveys that explore the consequences of corruption for firm behavior. Next, I summarize surveys that provide a window onto individual attitudes toward and experiences with corruption and dysfunctional government. Then I turn the causal link around and review studies that seek to determine the causes of poor government and corruption. Finally, I introduce distinctions between administrative corruption, "state capture", and what Michael Johnston calls "power chasing wealth" (2002).

A. The Consequences of Corruption and Poor Governance: Cross Country Research

Cross country research on corruption and governance is part of a growing body of research that looks for the institutional bases of economic growth. Measures of corruption and poor governance are correlated with per capita income and with the United Nations Human Development Index (HDI). Richer countries, on average, have less reported corruption and better functioning governments.[3] The same holds true for countries with high levels of the HDI, a measure that includes measures of health and educational attainment as well as a logarithmic measure of income. Figure 1 shows the relationship between the HDI and the index of corruption developed by Transparency International. Very high levels of human development are associated with low levels of corruption (high numbers on the TI index). However, high levels of corruption (between 1 and 4 on the TI index) are associated with a wide range of middle to low levels of human development.[4]

These two stylized facts raise the possibility that policymakers should forget about governance and just focus on stimulating growth though standard economists' prescriptions. Under that view, marginal improvements in governance are of questionable benefit to poor and corrupt countries, and good governance is a "luxury good" that citizens will demand once they are rich enough to care. However, the available statistical evidence suggests that, correcting for other factors, poor governance is itself one of the reasons that some countries are poor and have low or negative growth rates. Kaufmann and Kraay (2002) confirmed this result and, in addition,

found no positive feedback from higher incomes to improved governance. However, the issue remains contested. It seems plausible that both directions of causation hold. Demands for greater democracy, transparency, and integrity in government often become more insistent as per capita income rises. However, to the extent that corrupt rulers recognize this possibility, they have an incentive to limit prosperity to constrain such demands. Those who benefit from a corrupt status quo will try to impede reform. Improvements in human wellbeing seldom occur spontaneously but, instead, require government actions to complement private efforts. Governments that waste resources through malfeasance or inadvertence are a drag on growth and undermine the achievement of other goals.

: FIGURE 1

Mancur Olson's (1996) paper, showing that economic measures alone do a poor job of explaining the divergence in growth rates, spurred research on the importance of institutions. At around the time of the publication of that article, cross-country data ranking countries' institutional quality began to be available, and researchers interested in economic development began to use existing political science measures of democratization. This spawned a large literature showing that "institutions matter." I cannot summarize that literature here except to say that I am sympathetic to Dani Rodrik's (2003) view that first-order economic principles do not map onto unique policy packages; furthermore, as he argues, igniting growth and sustaining it over the long term are two different things and may require different polices. I focus here on work that incorporates a measure of corruption, recognizing that these indices reflect not just the level and frequency of bribes but also capture the general quality of state-business-society relations.

Transparency International (TI), an international organization that advocates for the control of corruption worldwide has published cross-country data on corruption since 1995. TI collects data from a number of different surveys that mostly report business and expert perceptions of corruption in various countries. Some of the underlying data sources also include questions concerning the overall business environment—asking about red tape, the quality of the courts, etc. Respondents rank the countries on a scale from excellent to poor. The annual TI indices are a compilation of corruption scores that average three years of data. They are ordinal rankings and do not provide measures of the volume of bribes, the incidence of corruption, or its impact. Because the underlying surveys included in the index vary from year to year, the data can not be used for time series studies. The World Bank (WB) has made use of the underlying indices that make up the TI index and has produced its own "graft" index using a different aggregation method and including more countries. It is highly correlated with the TI index. Most studies use one or the other of these indices. Although some countries change position from index to index and

have different rankings in the TI and WB data sets, there is an overall stability to the rankings. Furthermore, if a country's score differs from survey to survey, one cannot tell if this is because of the use of different sources, changed underlying conditions, or shifts in perceptions. Thus, these indices are a rough measure of the difficulties of doing business across countries, but they should not be used to make precise bilateral comparisons between closely ranked countries.

Studies using these data have found that high levels of corruption are associated with lower levels of investment and growth and that corruption discourages both capital inflows and foreign direct investment (Graf Lambsdorff 2003a, Mauro 1995, Wei 2000). According to Wei, an increase in the corruption level from relatively clean Singapore to relatively corrupt Mexico is the equivalent of an increase in the tax rate of over 20 percentage points. The statistical result holds for East Asian countries as well as for the others in his sample. Acemoglu, Johnson, and Robinson (2001) find that when the risk of expropriation is high, growth rates tend to be low. Most measures of institutional quality are correlated, and in this case, expropriation risk and corruption go hand in hand so that the same association holds for corruption. Countries perceived as more corrupt pay a higher risk premium when issuing bonds (Ciocchini, Durbin, and Ng 2003). Corruption lowers productivity, reduces the effectiveness of industrial policies, and encourages business to operate in the unofficial sector in violation of tax and regulatory laws (Ades and Di Tella, 1997; Graf Lambsdorff 2003b, Kaufmann, 1997). Graf Lambsdorff (2003a, 2003b) finds that an improvement in a country's TI corruption score by one point increases productivity by 4% of GDP and increases net annual capital inflows by 0.5% of GDP. This means that if a country such as Tanzania could achieve the corruption score of the United Kingdom, its GDP would increase by more than 20% and net annual per capita capital inflows would increase by 3% of GDP. Of course, such extrapolations are not to be taken strictly literally because the corruption score reflects all sorts of complex underlying conditions, but they do suggest the importance of the institutional environment to the achievement of economic success.

Highly corrupt countries tend to under-invest in human capital by spending less on education, to over-invest in public infrastructure relative to private investment, and to have lower levels of environmental quality (Mauro1997, Tanzi and Davoodi 2002a, Esty and Porter 2002). High levels of corruption produce a more unequal distribution of income under some conditions, but the mechanism may be complex—operating through lower investments in education and lower per capita incomes (Gupta, Davoodi, and Alonso-Terme 2002, Gupta, Davoodi, and Tiongson 2000). One study hypothesizes a U-shaped relationship. If corruption is very low or very high, inequality is low. However, in the high corruption case, everyone is equally poor. The empirical work, which omits the most impoverished countries, suggests that higher levels of corruption lead to increases in inequality, but the effect reaches a plateau at

very high corruption levels associated with low levels of per capita income. Corruption levels help explain Gini differentials within Latin America, the OECD, and Asia, but they do not explain the large Asia\Latin American differences in Gini coefficients or the intercontinental differences in growth rates (Li, Xu, and Zou 2000).

Corrupt governments lack political legitimacy (Anderson and Tverdova 2003). However, political supporters of corrupt incumbent governments, not surprisingly, express more positive views of the government. Presumably, this difference depends upon the individualized benefits that flow to these supporters. Surveys carried out in four Latin American countries (El Salvador, Nicaragua, Bolivia, Paraguay) in 1998 and 1999 showed that those exposed to corruption had both lower levels of belief in the political system and lower interpersonal trust (Seligman 2002). In Nicaragua, respondents were asked if the payment of bribes "facilitates getting things done in the bureaucracy." Interestingly, those who agreed that corruption gets things done were *less* likely to believe in the legitimacy of the political system (ibid. 429). Surveys of firms in countries making a transition from socialism provide complementary findings. Firms with close connections with the government did better than other firms, but countries where such connections were seen as important for business success did worse overall than those where political influence was less closely tied to economic success (Fries, Lysenko, and Polanec 2003).

In circumstances of low government legitimacy, citizens try to avoid paying taxes, and firms go underground to hide from the burden of bureaucracy, including attempts to solicit bribes. Using data from the World Values Survey and Transparency International, Uslaner (2003) shows that high levels of perceived corruption are associated with high levels of tax evasion with countries falling into two distinct groups. His survey data from Romania show that those who believe that one has an obligation to pay taxes have more trust in government. Similarly, Torgler's (2003) study of attitudes toward tax evasion in Central and Eastern Europe shows that when individuals perceived that corruption was high, they were less likely to say that people have an obligation to pay taxes. Thus, one indirect impact of corruption is to persuade people that it is acceptable not to pay taxes because government has been captured by corrupt officials and those who support them. As a consequence, corrupt governments tend to be smaller than more honest governments, everything else equal (Friedman, Johnson, Kaufmann, and Zoido-Lobaton 2000; Johnson, Kaufmann, McMillan, and Woodruff 2000). Thus in corrupt governments, the individual projects are excessively expensive and unproductive, but the overall size of the government is relatively small.

B. Business Surveys on the Consequences of Corruption

More nuanced results come from surveys that questioned businesses about the costs of corruption, red tape, and other constraints on doing business. The World Business

Environment Survey (WBES), carried out between the end of 1998 and the middle of 2000 under World Bank auspices, questioned several thousand enterprises in 80 countries (Batra, Kaufmann, and Stone 2003). Figure 2 indicates the way constraints on business differ between OECD members and emerging economies. In the statistical work using firm-level data, a high frequency of corruption, financing difficulties, high taxes, and lack of government/business consultation each had significant negative impacts on firms' sales growth over 1997-1999 after correcting for other firm-specific features such as private ownership, size, age, and export activity. In countries with negative scores on all four measures, the average growth of sales of existing businesses was more than 10 percentage points less than in countries on the positive side on all four. Investment growth was affected by four factors as well, with policy predictability replacing lack of consultation. The same was true for the four significant variables in the investment equation.[5] As the authors conclude, "While it may be difficult and take years to reform taxes, financing, corruption, and policy predictability, the evidence suggests that higher growth and investment are associated with such improvements".[6]

: FIGURE 2

Other less comprehensive research studied countries as diverse as those in Asia, sub-Saharan Africa, and Central and Eastern Europe. Most of this work is broadly consistent with the WBES survey. Survey work in Asia by the World Bank demonstrates the way government effectiveness affects the investment climate and hence both the level of foreign investment in a firm and the firm's export orientation. In Bangladesh, China, India, and Pakistan firm export levels and foreign investment were higher where hassles and delays were low. Given the evidence that endemic corruption is "sand" not "oil", that is another way of saying that corrupt pressures are low. To help one understand the magnitude of the effects, the authors report "that if Calcutta could attain Shanghai's level of investment climate, the share of firms …exporting would nearly double from the current 24% to 47%, comparable to the coastal Chinese cities. Similarly, the share of foreign-invested firms would increase by more than half, from the current 2.5% of firms, to 3.9%" (Dollar, Hallward-Driemeier, and Mengistae 2003: 7).

Svensson (2003) surveyed firms in Uganda. The level and incidence of bribery were positively associated with a firm's contact with the public sector for such matters as foreign trade, tax collection, and regulatory compliance. The level of bribes was a function both of the firms' ability to pay and of the expected cost of relocation. More corrupt firms had lower growth rates on average than others. This research suggests how corruption imposes differential costs on different types of firms and demonstrates how it is connected to the underlying policies of the government.

The most comprehensive survey work has been done in Central and Eastern Europe. The World Bank's two waves of surveys of the business environment in that

region document the specific ways that corrupt officials and intrusive rules affect businesses and show how corrupt environments impose costs (Hellman, Jones, and Kaufmann 2003, Hellman and Kaufmann 2004, Johnson, Kaufmann, McMillan, and Woodruff 2000). There are broad differences in corruption and protection payments between Russia and the Commonwealth of Independent States, on the one hand, and Central Europe, on the other. Formally organized firms in Russia and Ukraine are much more likely to admit to hiding sales and salaries than firms in Central Europe (Johnson, Kaufmann, McMillan, and Woodruff 2000, Table 1). Wholly off-the-books enterprises are more common in Russia and Ukraine, and such firms hide all of their output from the authorities. Furthermore, firms in Russia and Ukraine report spending more time on government and regulatory matters than elsewhere (18% and 25%, compared with about 10% for the other countries)(ibid., Table 2). This may be a rough measure both of the degree of extortion to which firms are subject and of the degree to which firms can be exempted from rules if they curry favor with authorities. In Russia and Ukraine almost all firms that answered the question report making illicit payments, and they hide a high proportion of their sales. In Central Europe, a group of firms also operates both corruptly and partly off-the-books, but the practice is not so widespread.

Surveys demonstrate how firms manage to cope when the legal system is weak. Informal relationships built on trust and private sanctions exist but cannot easily bear the entire burden of maintaining business deals. Weak states produce widespread corruption, private protection rackets, and the flouting of regulatory and tax laws. The countries of Eastern and Central Europe vary in the security of property rights, and countries with more secure property rights have higher levels of new investment by established firms (Johnson, McMillan, and Woodruff 2002, 2000).[7] The security of property rights is measured by the ability of the state to enforce its own rules impartially. In other words, the benchmark is not a libertarian state but one that provides services, regulates behavior, levies taxes, and operates an impartial court system. Property rights are less secure if bribery and protection payments are common and if the courts do not enforce contracts. Thus, corruption is not a route to a secure relationship with the state but opens up possibilities for extortion. Furthermore, if firms pay for protection, either to private mafias or to the police, this reduces the security of rights as well (Johnson, McMillan, and Woodruff 2002, Table 1). Trust in the state as a reliable actor seems important. Firms appear willing to substitute legal and impartially administered taxes for the uncertainties of bribe payments and the dangers of relying on private protection services (Friedman, Johnson, Kaufmann, Zoido-Lobaton 2000).[8]

C. Household Surveys

Surveys of individuals sometimes ask about attitudes toward corruption and bribery. The results provide a counterweight to those who claim that entrenched corruption

is acceptable to ordinary citizens. Interviews in a range of countries have found widespread popular disapproval of entrenched corruption (e.g., Anderson, Kaufmann, Recanatini 2003, Pasuk and Sungsidh 1994).

One particularly detailed study of four countries in Central and Eastern Europe provides some nuance (Miller, Grødeland and Koshechkina 2001, 2002). The research revealed that people disapprove of corruption even if they report engaging in it themselves. The authors conducted surveys and focus groups in four countries that cover the spectrum of transitional democratic and market institutions—from the relatively far-advanced Czech Republic, through Slovakia and Bulgaria, to Ukraine. Although experience with corruption varied markedly across the countries, the public's underlying values and norms did not differ greatly. A majority in each country expressed strong moral disapproval of payoffs, but, at the same time, a plurality of citizens in every country except the Czech Republic said they would pay a bribe if asked. The authors conclude that the basic problem is not a weakness in the underlying values of citizens and public officials but an excess of corrupt opportunities. Because of a concentration of corrupt opportunities in some areas of public life, the officials most likely to receive gifts or bribes are hospital doctors, traffic police, and customs officials. One hopeful finding— reproduced in table 1—was that people's attitudes toward bribery were affected by their perceptions of others' actions. Attitudes are not deeply entrenched but depend on situation-specific variables, such as one's perception about whether or not others are paying.

: TABLE 1

In diagnostic exercises conducted by the World Bank, surveys of this type have been used to narrow down anti-corruption efforts to areas of most concern to the population. However, although these surveys isolate pressure points where corruption is widespread, they do not measure the cost of bribery in terms of the inefficient or unfair allocation of public services or burdens. The next step in the diagnostic exercise, therefore, should be an estimate of the relative costs of tackling different types of corruption that affect daily life.

D. Causes of Corruption and Poor Governance

Given the costs of corruption and poor governance, reformers need to isolate the causes of these phenomena. Cross-country data permit one to obtain a broad overview of the underlying causes of corruption and weak governance. I have already mentioned the role of income and wealth as both a cause and a consequence of corruption. That association is clear in all the studies cited below. However, the simultaneity often is not well handled in the empirical work. Nevertheless, it seems possible to conclude, first, that poor governance contributes to low growth and to the other harmful outcomes noted above, and that weak underlying economic conditions

facilitate corruption. The exception is a very poor country with weak institutions that is so badly off that there is little for anyone to steal.

Some studies find that trade openness and other measures of competitiveness reduce corruption (Ades and Di Tella 1999, Sandholtz and Koetzle 2000, Blake and Martin 2002), suggesting that societies with fewer rents to share are less corrupt. However, once again the causation is unclear; countries that do not favor corrupt firms may be able to establish a policy of open and competitive markets. Graf Lambsdorff (2003a), for example, finds that weak law and order and insecure property rights encourage corruption which in turn discourages foreign capital inflows.

Inequality contributes to high levels of corruption. In democracies in particular, inequality facilitates corruption, a result consistent with the state capture variant of corruption. The negative effect of inequality on growth may be the result of its impact on corruption taken as a proxy for government weakness (You and Khagram 2004). Here too the causal arrow goes both ways.

Historical and social factors help explain cross country differences. For example, Acemoglu, Johnson, and. Robinson (2001) use the mortality rates of European settlers as an instrument for the type of colonial regime put in place by the imperial power and find that it does a good job of predicting expropriation risk (and corruption levels) at the end of the twentieth century. La Porta, Lopez-de-Silanes, Shleifer, and Vishny (1999) consider legal origin, religion, ethnolinguistic fractionalization, latitude, and per capita income as determinant of a range of features of economic, social, and political life. Corruption, as well as other measures of institutional weakness, is worse in countries with higher ethnolinguistic fragmentation, few Protestants, and Socialist or French legal origins. (See also Sandholtz and Koetzle 2000, Treisman 2000.)

Colonial heritage, legal traditions, religion, and geographical factors seem associated with corruption and other measures of government dysfunction, but these are not policy variables that present day reformers can influence. The key issue is whether these historical regularities directly affect government quality or whether they help determine intermediate institutions and attitudes that present day policies can affect. In La Porta, Lopez-de-Silanes, Shleifer, and Vishny (1999) the historical variables are not always significant and become entirely insignificant when they add income and latitude. Thus, these historical patterns may operate through their impact on underlying institutional structures, not as direct determinants of corruption. If so, that may be good news for reformers so long as there are alternative routes to the creation of institutions that facilitate economic growth and high income (cf. Rodrik 2003). Latitude and history need not be destiny.

The impact of democracy on corruption is complex. High levels of economic freedom and lower levels of corruption go together as does an index of democratization (e.g., Sandholtz and Koetzle 2000, Blake and Martin 2002, Kunicova and

Rose-Ackerman 2003). Governments with more female participation in politics are less corrupt, and this is consistent with survey evidence suggesting that women are more disapproving of corruption than men (Swamy, Knack, Lee, and Azfar 2001, Crook and Manor 1998: 42). Within the universe of democracies, features of government structure, such as presidentialism, closed-list proportional representation, and federalism, facilitate corruption (Kunicova, 2002; Kunicova and Rose-Ackerman, 2003; Treisman, 2000).[9] Presidential systems that use proportional representation (PR) to elect their legislature are more corrupt than other types of democracies. Many parliamentary democracies that elect legislatures by plurality rule have a heritage of British colonial rule, and many PR systems had French or Spanish rulers. Present day levels of freedom also have historical roots. However, if constitutional form, protection of rights, women's rights, and electoral institutions are important determinants in and of themselves, then countries have policy levers available even if they cannot change their histories.

A World Bank survey permits one to see how one country compares with others on a range of different factors (Kaufmann, Mastruzzi, and Zavaleta 2003: 363-364). Although broad measures of corruption, government quality, and informal sector activity are strongly correlated, more fine-grained analysis often shows pockets of strength and weakness. For example, a study of Bolivia, using this survey, showed that it ranks poorly on several measures of corruption, judicial quality, and property rights, but rather well on standard macro-economic variables such as inflation, the exchange rate, and the quality of the central bank. Because Bolivia has had a low growth rate, the results suggest that getting the macro-economics fundamentals right is not sufficient. Institutional reforms are needed, and within Bolivia itself some public institutions score better than others and may provide reform models (ibid. 364-365).

E. Crony Capitalism and the Links between Political and Economic Power

The World Bank distinguishes between administrative corruption and what its calls "crony capitalism" or "state capture" Country-specific research on such countries as Russia, Albania, Indonesia, and Malaysia confirms the importance of the distinction. Administrative corruption includes the use of bribery and favoritism to lower taxes, escape regulations and win low-level procurement contracts. "State capture" implies that the state itself can be characterized as largely serving the interests of a narrow group of business people and politicians, sometimes with criminal elements mixed in. Even if the group with influence changes when the government changes, most of the citizens are left out. Michael Johnston (2002) proposes a richer taxonomy that includes political systems that manipulate private firms for personal gain. He calls this "power chasing wealth" as opposed to "wealth chasing power." The World Bank would probably put both types in the "state capture" category, but they

may have different implications. For example, Russia may be moving from a case where private wealth controlled public power to one where political power dominates private wealth.

Favored firms may not have secure property rights in the legal sense but may be able to obtain favored treatment because of their insider status (Hellman, Jones, and Kaufmann 2003). The main risk facing such firms is the risk of a change in the political leadership. For example, in a study of Indonesia under President Suharto, Fisman (2001) used an index of the political connectedness of firms listed on the Jakarta Stock Exchange, dubbed the Suharto Dependency Index. He demonstrates that rumors about Suharto's health problems between 1995 and 1997 had a more negative impact on the share prices of firms with high levels of this index and that the differential impact was greater the worse the rumors.[10]

The World Bank and the European Bank for Reconstruction and Development show that, although administrative corruption is a problem throughout the former Communist states, state capture is a particularly serious problem in the countries of the former Soviet Union. In such situations the firms that do the capturing perform well, but overall economic growth suffers (Hellman, Jones, and Kaufmann 2003). Fries, Lysenko, and Polanec (2003: 31-32) document the differences between "captor" firms with insider status and "non-captor" firms. The former have higher growth rates of fixed capital, revenue, and productivity. Slinko, Yakovlev, and Zhuravskaya (2004) obtain similar results using data from the Russian provinces.

If top political figures themselves exploit their position for private gain, the effectiveness of government programs and the impact of foreign aid and lending suffer. Even if those with good political connections are also good economic managers, there is a long term risk that they will exploit their dominant positions to squeeze out potential competitors (Acemoglu 2003). This inequality of influence can extend beyond special treatment by the executive and the legislature to include the courts as well.

World Bank researchers define "crony bias" as the difference between the reported influence of one's own firm and business association, on the one hand, and the influence of those with close ties to political leaders, on the other. In a study using firm level data from the 2002 Business Environment and Enterprise Performance Survey on former socialist countries (BEEPS), Hellman and Kaufmann (2004) find that firm managers who believe that the state is unduly influenced by a narrow set of "cronies" are more likely to withhold taxes, pay bribes, and avoid using the courts. These actions then help keep state institutions weak. Bribery and extortion are mostly a problem for medium-sized businesses. Large dominant firms have close relationships with top political leaders so that mutually beneficial deals are possible. These deals are often harmful to the overall growth and prosperity of the country and undermine efforts to establish the legitimacy and trustworthiness of the state.

In the geographically broader WBES survey of 80 countries there is a marked relationship between this measure of crony bias and survey responses on the size of the unofficial economy and the decree of democratic voice and accountability. A large unofficial economy indicates that the regulatory and taxation powers of government are low and that many firms cannot obtain outside financing because they are off the books. Low levels of voice and accountability suggest that the state is not responsive to its citizens' interests. Figures 3 and 4 present these results.

: FIGURES 3, 4

II. Reform Proposals

Research on the causes of corruption suggests ways to think about reform. First, the simultaneity between income and poor governance implies that purely economic prescriptions, taken alone, will not succeed either in promoting growth or in improving government performance. If, as Kaufmann and Kraay (2002) argue, causation flows mostly from corruption to low levels of income and growth, that conclusion is strengthened. Macro-economic policy prescriptions presuppose a well-functioning government, which is just what is lacking in corrupt countries. Similar problems of simultaneity exist for trade openness and inequality. Thus proposals to improve governance by concentrating on economic growth, trade openness, and reductions in inequality beg the question of how weak states could accomplish such fundamental changes. Second, history and latitude may be important, but they are givens, not policy tools. One needs to determine what they are instruments for and whether present day institutions are subject to reform whatever a country's history. Third, some features of political systems seem to promote honest and effective government: high levels of economic freedom, parliamentary structure, certain types of electoral institutions, and avoidance of private capture of the state and of state capture of the economy. Some of these statistical associations could be translated into particular policy proposals, but most of them are at a level of abstraction that is not easy to operationalize. Because the associations are statistical regularities based on cross-country research, I am reluctant to translate them into concrete proposals. My own emphasis is on middle-range proposals that concentrate on particular sectors and deal with government accountability from the bottom up. They are consistent with the broad empirical regularities outlined above, but they have a more selective focus.

The net benefits from some specific anti-corruption reforms seem to be quite high. Weighting benefits and costs more highly if they are experienced by the poor would only enhance the value of most policies. The problems are, first, setting priorities for a long term response and, second, overcoming the resistance of those

who benefit from the status quo. Often even if the net benefits are large, the beneficiaries of the status quo are very powerful (Krastev and Ganev 2004, Fries, Lysenko, Polanec 2003).

The priorities I establish are based on my belief in some stylized facts and obviously depend on the truth of my empirical hunches. My empirical hunches are the following. (1) To the extent that low corruption is associated with beneficial outcomes—stronger growth, higher incomes, more equal income distribution—the explanation is not corruption taken in isolation but rather the close correlation between corruption and other measures of the way government functions.[11] (2) From this, it follows that policies to improve government functioning should not primarily focus on enforcing criminal laws against corrupt dealings. These laws are a necessary background condition but will mean little unless accompanied by more systemic reforms. (3) Instead, one must consider the underlying institutions and habits of behavior that make corruption endemic in some countries and in some sectors but not others. (4) Although norms of behavior with historical and social roots influence the level of corruption, corruption is also a crime of opportunity that requires willing participants on both sides of the transaction. Variations in corruption within a country suggest that this is so. Thus, a country's legacy of corruption and poor governance need not be accepted as somehow determined for all time. The situation can be improved on a case by case basis. (5) Political and bureaucratic corruption occurs where greed and self-interest interact with government institutions. However, different factors create corrupt incentives in each case, and hence they need different policy responses.

Corruption, standing alone, is not comparable to hunger, disease, and violence among the world's problems. However, if the weak government capacities of which it is a symptom persist, targeted policies will fail in weak and dysfunctional states. This is especially so when a central state is under the control of a narrow group that does not operate in the interest of most of the population. Government may also be dysfunctional because it is excessively decentralized so that lower-level government officials can establish local monopolies free of oversight from higher levels of government. Rather than deal with the problem of concentrated political power head on, my options focus on ways to constrain and limit such power while at the same time acknowledging the value of a competent, well-functioning state.

The largely negative finding of a study of reform efforts in Eastern and Central Europe provides support for my approach (Steves and Rousso 2003). The WB and the EBRD carried out surveys of businesses in that region in 1999 and 2002. These are not panel studies, but they do shed some light on changes in the business environment over time. The survey results were matched with country level measures of anti-corruption initiatives that took the form of an index combining: (1) domestic

legal reforms designed to increase transparency and accountability, (2) ratifications of anti-corruption conventions, and (3) specific anti-corruption actions such as publication of an anticorruption strategy and action plan and the establishment of an anti-corruption commission. In general, those countries that were least corrupt in 1999 adopted more of these reforms during the time period, partly in response to European Union pressure. Scoring high on the index, however, was not a reliable predictor of reductions in reported corruption and, unfortunately, was also associated a perceived increase in the problem. These results need to be interpreted with caution because they cover only a short period of time and one region of the world. They do, however, suggest that policies that simply raise awareness will not have the desired effect unless they are accompanied with more concrete, substantive changes in state/society relations.

Based on existing research and my own view of the way the parts of the good government puzzle fit together, I have isolated the following policies for further discussion. They are complements, not substitutes. Where possible I discuss studies that highlight successful policies and analyze failures. Some states are so dysfunctional that none of these reforms makes sense. My candidate for the most misguided World Bank project was one designed to improve President Mobutu's tax collection capacity in Zaire. Obviously, such a "reform" would not have improved social welfare. Leaving such deeply dysfunctional states to one side, the policies I discuss are: (1) improved oversight and participation by citizens and greater government transparency, (2) procurement reform, (3) improved revenue raising capacity, (4) improving the business environment by cutting unnecessary red tape, and (5) international efforts involving multinational firms and international organizations with a focus on asset recovery and greater transparency in international natural resource contracts.

Some reforms could, in principle, produce measurable improvements in productivity and economic growth; others, however, enhance government legitimacy and accountability and have no straightforward financial counterpart. However, as I demonstrate below, quantitative studies in individual countries demonstrate that empirical work can provide strong guides to policy. Thus, all of my specific policy proposals are accompanied by ideas for improving the quantitative bases for policymaking. This research usually will require primary data-gathering efforts, but in highly corrupt environments, the payoffs can be substantial.

In some countries corruption of the police and the army reflects the role of organized crime in society. That kind of "state capture" is obviously a major problem for the states involved and for those harmed by illegal businesses such as drugs and trafficking in humans and weapons. However, because it raises a host of issues specific to the control of organized crime and illegal businesses, I will not discuss this type of corruption here.[12]

A. Oversight and Transparency

> "[C]orruption is an institutional system in which rights are dissolved in exchange for gifts…." Robbins (2000: 440).

Survey data from 80 countries suggests an association between low levels of voice and accountability and low levels of per capita income (figure 6). Furthermore, as figure 4 indicates, when voice and accountability are high, "crony bias" tends to be low. However, that relationship does not hold when a country moves from very low to low levels of voice and accountability. Thus, if reforms raise expectations through pure participatory strategies, they may produce disillusionment if not coupled with more fundamental changes. At this level of aggregation, however, one cannot make specific policy proposals. Instead, I move down a notch and consider the benefits of a particular type of citizen oversight and government transparency: local citizen involvement.

: FIGURE 6

The benefits of moving to more local control depend both on the effectiveness of such control and on how bad things are at present. There are two prongs to the development of a strategy. First, one must find programs and governments that are very wasteful in providing services or managing aid flows, and second, within that universe, one must select countries and projects suitable for managed decentralization. By this I mean, decentralization of monitoring and service provision along with centralized information flows and the enforcement of anti-corruption and anti-fraud laws.

Several detailed studies have examined the way local involvement in public programs can enhance efficiency and increase benefits. They show that it can be done, but also provide numerous cautionary tales of poorly designed programs. I concentrate on the conditions for successful decentralized programs, recognizing the need to guard against the capture of state structures by those seeking illegal enrichment. Careful studies of individual programs suggest that the benefits of improved integrity in local aid projects and public service delivery ranged from 100% to 400% in the cases studied. However, the more anthropologically informed work suggests limits to participatory models in hierarchical rural societies. Decentralization can be an invitation to local corruption and self-dealing if not managed effectively.

In Latin America reformers have made numerous attempts both to involve rural people in the design and monitoring of agricultural development programs and to increase the participation of city dwellers in government decision making. The rural development programs sought to improve the targeting of programs to the needs of farmers and to increase accountability to beneficiaries (Das Gupta, Grandvoinnet,

Romani, 2000; Parker, 1995). The urban cases, of which the most famous is Porto Alegre, Brazil, had the explicitly political goal of increasing democratic participation in opposition to existing clientalistic structures (Abers, 1998. de Sousa Santos, 1998). The successful cases in both settings gave citizens better information about what to expect from government and developed their capacity to hold public officials to account. The result was a reduction in corruption and self-dealing.

The World Bank's surveys of public officials in Bolivia provide some statistical backing for the view that low corruption and high levels of transparency and "voice" are beneficial to the actual performance of government and help the poor (Kaufmann, Mastruzzi, and Zaveleta 2003: 380-388). A study based on 1200 interviews with public officials in many different national agencies and local governments demonstrated wide inter-agency and inter-government variation. Using simultaneous equation techniques, the study found that public service delivery is negatively associated with corruption and positively with the external voice of users and with transparency. Bribery and corruption are higher in more politicized units of government and in those with lower transparency and less meritocracy. Transparency is affected positively by voice and negatively by corruption and politicization. Municipal governments perform worse than central government agencies on average but do sometimes provide better access for the poor. Measures of civil service management and individual ethical commitments had no independent impact although they may obviously be associated with some of the other data (ibid.: 383). Figure 7 illustrates one result—the finding that higher levels of voice and accountability are associated with greater accessibility of the poor to public services (Kaufmann 2003: 24).

: FIGURE 7

Survey evidence and case studies of participatory programs suggest that they require a long-term commitment from established governments along with technical and organizational help. For example, case studies of USAID Community Partnership Grant Programs in South Africa found that successful programs had broad-based involvement combined with support from the incumbent local government. The one clear failure was when USAID worked with a defeated politician whose efforts were undermined by those in power (Adams, Bell, Brown 2002). Trevor Brown (2001) documented the importance of technical assistance in developing local government capacity in Ukraine and cites other supportive results from around the world. People who are not used to political power need time to learn how to exercise it responsibly. A 1998 study reports that over eighty Brazilian cites have begun to adopt some form of participatory budgeting (de Sousa Santos 1998). This suggests that one could review these efforts to see which ones worked and which failed.

One positive examples comes from work by Ritva Reinikka and Jakob Svensson (2002, 2004a, 2004b). They document the severe leakage of central government funds meant for local primary schools in Uganda. One dollar of central government funds produced $.20 in budget for local schools. Their study led to a simple, information-based reform that had positive results. Reform focused on publicity combined with better monitoring. After its introduction, one dollar expended by the center produced $.80 of local school funds, a 400% increase. Nearly 75 percent of the improvement in the targeting of funds can be explained by a newspaper campaign to publicize funding levels so that parents would know what funds their children's schools were due to obtain (Reinikka and Svensson 2004a, 2004b). Importantly, parents were already organized and able to exert pressure. Mere publicity will not work in isolation. The study gives no estimate of the cost of newspaper advertisements and notice boards, but they must have been minimal. The most substantial costs were increased official monitoring and the time spent by parents in checking on the school budgets. Because 20% is still lost, the returns on a dollar of actual education spending would need to be at least 12.5% for the returns to the central government on the program to be 10%. Before the reform, however, the returns would have needed to be 50%! Thus, the program appears to be cost effective although it also has an upper bound—losses will never go to zero. A key feature of the Uganda case, however, is the existence of parent-teacher groups at the village level that can perform monitoring. In countries where such groups do not exist or where powerful local or regional actors can steal with impunity, more costly and complex interventions will be necessary. Even in Uganda, education may be a special case because it is a service used by school-age children on a daily basis, unlike, say healthcare, where demand is more episodic, and sick and injured users are vulnerable to exploitation.

Uganda provides a "best" case scenario. Conditions were very bad ex ante, and once research revealed the shortfall, a centralized information provision policy combined with better enforcement reversed the percentages. This reform does not answer the question of how much a country ought to spend on education but suggests that, with the reform, education spending will appear to be more productive. This result may lead to an increase in the budget. Suppose, just for the sake of illustration, that the extra costs of the anticorruption program are $.10 for every dollar of appropriated funds, then every $100 of budget would produce $100-$10-.2($90)=$72 of education spending, up 360% from before the reform. Of course, as noted above, these are only pecuniary gains so one would also want to know how many resources were wasted hiding the fraud and the rate of return on education compared to the use of the diverted funds. At the very least, however, the distributive impact of the reform is in favor of children, many with low income, and the gains are very large if one takes as given the share of the government budget going to education.

To perform a cost\benefit analysis of this reform, one would need an estimate of the rate of return to primary education spending in Uganda. Unfortunately, such data are not available. However, in wealthy countries returns to an added year of education are in the range of 8-12% in increased earnings for individuals. Because these estimates ignore public benefits from an educated citizenry, social benefits ought to be larger. Recent attempts to measure the impact of education on economic growth have produced disappointing results in the developing world, suggesting that years of education are not a good predictor (Easterly 2001: 71-84). Jere Behrman (2003) in a review article argues that older studies showing high returns to education in poorer parts of the world overstate the private and public returns to schooling. Perhaps the disjunction between the results for individuals in developed countries and cross-country studies lies in the fact that a year of schooling in a poor country may not mean much in terms of actual learning if corruption and self-dealing lead schools to operate poorly. Easterly refers to absent teachers and school officials who sell school supplies for person gain. Literacy levels would surely be higher if these illegal practices could be curtailed. The study in Uganda suggests that simple theft of resources by regional officials was the reason for underfunded schools. If theft is high, years in school may be a poor proxy for learning.

Other instructive cases concern the devolution of authority in Nepal, India, Bangladesh, and Indonesia. In Nepal and Karnataka, India, researchers estimated that the productivity of external aid funds doubled as a result of more local control. The programs were of direct benefit to local people—roads, irrigation projects. Thus, they had a reason to assure that funds were used effectively. However, research in Rajasthan and Tamil Nadu in India, Bangladesh, and Indonesia highlight the need to give careful consideration to local conditions to avoid failure.

In Nepal, a pilot program involved local people in the direct administration of a food-for-work program through information diffusion and a workable structure of monitoring. Standard practice involved national government guidelines for paying workers that were far above market wages. As a result, contractors with the national government, paid market wages and pocketed the difference. When control was transferred to a sample of villages in an experiment, they paid market wages and build twice as many miles of roads with the same budget. The result was a dramatic increase in the cost-effectiveness of aid programs and a large increase in client satisfaction. The costs were the time spent by the villagers in administering the program as well as the cost of technical assistance to establish the system. However, presumably there are corresponding savings at the national level where bureaucratic inputs could be reduced. The main issue in such cases is how to generalize the positive experience in an experiment to the country as a whole. Key questions about the relationship between local authorities and the national administration are not answered by positive experiences in a few villages. In fact, in Nepal efforts to expand

the program met with resistance as national level officials and private contractors mounted resistance (Meagher, Upadhyaya, and Wilkinson, 2000).

In Karnataka, India, decentralization improved government performance and limited corruption according to fieldwork done in 1978-79 and 1981 (Crook and Manor 1998: 22-84). Public sector workers, especially teachers, worked harder because they were, in the words of one person interviewed, "under the supervision of the questioning public mind" (ibid.: 60). Absenteeism continued to be a problem, but those who did come to work performed better. Although the number of people involved in corrupt acts increased, they siphoned off fewer resources (ibid.: 61). Before decentralization "a large fraction" of funds was diverted. The Indian decentralization policy increased the number of officials (elected and otherwise) from over a score to 3000. This increased the number of potential bribe takers. However, the greater transparency of the political process limited the overall level of payoffs. A vigilant press, an active two-party system, and effective voluntary organizations contributed to transparency. For a given level of funding from the center, there was a large increase in micro-level infrastructure projects. The authors conclude that this increase resulted both from the preferences of local political actors for such projects and from a decline in corruption. Under the decentralization policy corruption took from 5 to 25 percent of local government funds with most districts falling in the 5 to 10 percent range. Only in 2-3 remote districts was the share 25 percent. This was a major improvement over the past. However, although overall corruption decreased, most people believed that it had increased because of the greater transparency of government operation (ibid.: 79).

On the down side, increases in local control do not necessarily increase transparency and accountability but might instead promote locally based corruption and even facilitate organized crime influence (Anderson, Kaufmann, and Recanatini 2003: 11, Das Gupta, Grandvoinnet, and Romani 2000, Gong 2002). In a worst case scenario, devolution enhances the power of local patrons and entrenched interests. For example, an interview-based study of forest management in the Indian state of Rajasthan demonstrated the way a de jure institution transformed into a stable system of extra-legal exchanges (Robbins 2000). Robbins reports the range of de facto prices for various uses of the forest and explains how personal connections interacted with payoffs to favor some individuals and families over others. As a result, many of the national conservation goals are unmet with some species of trees and wildlife becoming particularly endangered. Households lost the ability to complain because of their own complicity. Increased "oversight" would have been ineffective. According to Robbins, nothing will change without a change in local power relations (ibid.: 434-435, 439-440).

Consider also an experiment in Bangladesh (Crook and Manor 1998: 85-135). Here an effort to decentralize political decision-making increased corruption and

increased the inefficiency of public works spending. According to the authors, "corruption assumed major proportions, so that the councils would need to receive huge injections of funds if significant amounts were to be left over for development after profiteering" (ibid.: 112). Based on interviews and their own observation, the authors estimate that perhaps 30 to 40 percent was stolen (ibid.: 119). Notice that if the funder wants a rate of return of 10% on its money, then the underlying project would have to earn 14 to 17%. The authors attribute the high rate of corruption and theft not only to the venality of local leaders but also to the permissive attitude of higher authorities.

In Tamil Nadu in the 1980s and 1990s investments in tank irrigation systems were supported by overseas aid through procedures that encouraged the formation of local Water User Associations (WUAs). The WUA's were to contract for work, organize construction, and manage the improved systems using resources from new community rights over local resources. An outside team supported each WUA including a technical assistant, an institutional organizer, and a process documenter (Mosse1997: 268). Mosse details the caste and other conflicts in the WUAs and the way the WUAs were embedded in local social structures. They became a locus for conflict, not a site for reform. The actions of the WUAs were, according to Mosse, driven by the priorities of outsiders as much or more than the wishes of village residents.

Finally, in Indonesia, another study documents how resources were wasted through corruption and self-dealing in village-level aid projects and suggests some ways of involving the beneficiaries in monitoring the programs using existing local institutions such as local Muslim prayer groups (Woodhouse 2002). A further study of the way local communities and the state dealt with allegations of corruption in Indonesia stresses the interactions between local processes and the state. Local procedures to recover corruptly obtained funds were successful in many cases but often only because of the threat of going to the courts. Outside actors involved in the administration of aid programs or willing to provide legal help for free were often essential to persuade local people to pursue a case against powerful local individuals. Even in such cases, however, court judgments were difficult to enforce, and even if an official went to jail, the lost funds were not recovered. Because of the distance of the courts from remote villages, once a case entered the formal legal system it lost salience at the village level (World Bank 2003).

In evaluating these cases, one must, of course, recognize that money lost to corruption and self-dealing is not burnt up. It is used for something. Individual officials and their families are better off with more money in their pockets. A pure cost/benefit analysis is agnostic about who obtains the benefit and looks only at net total gains. The analyst would compare the marginal productivity of the corrupt transfers with the marginal productivity of the public project before recommending reform. However, this is, in my view, a fundamentally misguided way to approach the issue.

If, indeed, funds are more productive in private hands, then the government should simply discontinue the program, not condone corruption. At the very least corruption and self-dealing require wasteful efforts to keep malfeasance secret, skew the distribution of benefits and costs, and encourage the use of resources to compete for rents, rather than to engage in productive activity (Krueger 1974, Rose-Ackerman 1999: 9-15, 213-215). If one cannot locate feasible anti-corruption strategies for very ineffective programs, simply canceling the program is always an option.

The cases suggest that there are two ways for grassroots involvement to limit corruption both of which appear promising. First, local households can monitor the use of central government or foreign aid funds and report to the government when they observe misuse. This can produce very large gains if the status quo is characterized by large leakages at the center. Second, local people can actually provide the services themselves under contract with an aid agency or a higher level government. Both of these options require that the public service be one that is actually desired by the local people; otherwise the benefits will be limited to jobs and supplies, and few services may be provided as people accept sinecures and walk off with materials. The options also require local organizational structures that are relatively effective and egalitarian. Even if these two conditions hold, the interaction between the grassroots and higher levels of government needs to be analyzed to be sure that empowering the local level is actually a sustainable goal. In short, these encouraging successes are not capable of mindless generalization although one can surely find other cases beyond those outlined above where they can work well.

The rich variety of experience is both encouraging and humbling. The cases indicate which factors need to be considered but can hardly produce the "blueprints" or "best practices" preferred by the international lending organizations. Existing research suggests that a number of factors must come together before government reform can succeed. Transparency and publicity are powerful tools but only if combined with grassroots organizations with the incentive and the competence to use the information provided. Outsiders can help both in providing information and in helping construct functioning local organizations. These strategies will not work, however, if state officials use intimidation and threats to keep ordinary people from engaging in oversight and political action. Formal state institutions such as the courts, the Ombudsman, a functioning Freedom of Information Act, and an independent Audit Office, need to form a backstop for efforts to make government more transparent and accountable to ordinary citizens. It does not do people much good to know what the government is doing if they are too intimidated to act on this information or if the routes for protest are blocked or ineffective. An outline for reform in this area would include both efforts to improve accountability at the grass roots in small towns and urban neighborhoods and the strengthening of central government institutions that provide accountability.

However, even if effective programs can be designed, they cannot deal with corruption that is not subject to monitoring by individuals. I turn now to two areas where grassroots efforts are not sufficient: procurement and revenue collection.

B. Procurement Reform

Business executives worldwide believe that corruption in public procurement contracts is prevalent although there is considerable interregional and cross-country variation. The 2002 Executive Opinion Survey of the World Economic Forum shows the proportion of those surveyed who report that bribery is high/very high in various areas of business life including corruption in procurement (figure 8). Some business people report that they avoid government business for that reason (Kaufmann 2003: 8-9, Anderson, Kaufmann, Recanatini 2003: 11-13). Of course, corruption in contracting occurs in every country— even those at the high end of the honesty index such as Scandinavia, Singapore and New Zealand, but it appears more widespread and harmful in some countries than in others.[13] This is partly a function of the share of business in government hands. Two countries might have corruption in 20% of all public construction contracts, but if the public sector accounts for 80% of construction in one state and 10% in another, the private construction sector's perception of the level of bribery will likely be affected by this difference.

: FIGURE 8

"Grand "corruption involving major construction projects can increase costs and distort priorities. If the cost of a project is inflated by ten percent as a result of corruption, the rate of return on many projects will fall so low as to make the project not worth pursuing. Furthermore, some projects would not be worthwhile with zero corruption; they are only on the government's agenda because of the kickbacks provided. In other cases, the project provides net benefits if payoffs are zero, and the important issue is the link between bribe payments and the rate of return on the project. Do the bribes just lower the profits earned by contractors in oligopolistic markets, or are they shifted to taxpayers? We have no good estimates of the incidence of bribes, but only under extreme conditions will contractors bear the full burden. Systemic corruption of this kind reduces competitiveness by limiting the number of bidders, favoring those with inside connections over the most efficient candidates, limiting the information available to participants, and introducing added transactions costs. If top officials, including the head of state, are concerned primarily with maximizing personal gain, they may favor an inefficient level, composition, and time path of investment. Investors' decisions may also be affected by the fact that they are dealing with political leaders.

Consider the officials' decision calculus. The impact of high-level corruption goes beyond the mere scale of public investment and lost revenue for the public budget. Top officials select projects and make purchases with little or no economic rationale. For

example, if kickbacks are easier to obtain on capital investments and input purchases than on labor, rulers will favor capital intensive projects irrespective of their economic justification. One empirical study demonstrates that high levels of corruption are associated with higher levels of public investment as a share of GDP, less productive public investment, and lower levels of total investment (Tanzi and Davoodi 2002b). Corrupt rulers favor capital intensive public projects over other types of public expenditures and will favor public investment over private investment. They will frequently support "white elephant" projects with little value in promoting economic development.[14] The demand for cement is one tip-off and might be used as a rough measure of excess public construction. For example, in Italy the annual per capita consumption of cement has been double that of the United States and triple that of Germany and Britain. A review of the "Clean Hands" corruption cases in Italy reveals that many construction projects were poorly conceived, over-priced, and had little or no justification beyond their ability to produce kickbacks (della Porta and Vannucci 1999).

Using the Italian case, Miriam Golden and Lucio Picci (2004) demonstrate that more precise measurement is possible. They use a study that finds that, across the Italian regions, corruption has a negative effect on economic growth by reducing private investment and reducing the efficiency of public investment (Del Monte and Papagni 2001). Golden and Picci provide evidence on one important type of inefficiency—excessively costly public investment projects. They combine measures of physical public capital stock in the Italian regions with measures of cost to produce estimates of the relative efficiency and inefficiency of public spending throughout Italy. Building on research that finds that corruption and waste go together, they assume that corrupt officials encourage wasteful projects as a way of generating rents. The physical data cover a range of government capital investments in 1997, including roads, railroads, hospital beds, and number of school classrooms, combined into an index that is expressed as a ratio to the national average. They use a perpetual inventory model that adds up past capital formation and deducts assets when they reach the end of their service lives. The financial measures are then corrected for inter-regional cost differences and normalized so that the country mean is set at one.[15] Overall, the physical index favors the northern part of the country, and the financial index favors the south. The ratio of the two indices is a rough measure of the relative levels of corruption and inefficiency. Figure 9 is a map of Italy with the regions shaded from dark to light with darker regions representing lower values of this measure. The index has a .82 correlation with Robert Putnam's (1993) measure of regional governments' institutional performance and a correlation of minus .66 with legal charges of high-level legislative malfeasance.

: FIGURES 9, 10

Of course, these are just indices that range from 1.7 to .2. They do not translate directly into a cost/benefit ratio. However, if the statistical work has corrected for

other reasons for interregional variation, these results indicate that there are large potential gains either from reducing waste and corruption in the poorly performing regions or from transferring funds to the high performing regions. Unfortunately, the poorly performing regions also tend to be the poorer regions (figure 10). Hence, a shift of funds would be regressive. Nevertheless, within the group of low per capital income regions the state might announce its willingness to allocate future funds on the basis of past performance. Because the ratios are based on stocks, not flows, the state would also need to be able to calculate flows over a two or three year period. Within individual countries it could help national policymakers see where the pressure points are. In Italy regions that are more efficient (less corrupt) than expected given their income are above the regression line in figure 10.

As a thought experiment, suppose that we interpret the data as measuring productivity in the sense that one dollar spent in the region with the mean score produces one dollar's worth of output. (Of course, it is possible that the mean represents either a high or a low level of absolute output per dollar of input). Suppose we take the goal of raising the ten lowest regions up to the mean. If productivity in all these regions could be improved to equal the present country mean, this would imply that a hundred dollars invested in these regions would yield 100 dollars of output instead of $53.90, an increase of 86%. Even if omitted variables related to real resource costs explain half the difference, the increase would be over 40%. Of course, the same caveat applies as with the education example above. A full cost\benefit analysis would need an estimate of the social benefits of spending on infrastructure. However, once again, for a given infrastructure budget, output could be increased either by relocating the funds or by reforming the production process in weak regions.

Given the work of Golden and Picci for Italy, one might replicate this work in other parts of the world to permit rough estimates of the variation over regions, states, or metropolitan areas in the productivity of public spending. These results can then be used to allocate public funds in a way that gives sub-national governments an incentive to use funds efficiently. Such a policy, however, leaves the actual reforms to the sub-national governments. Thus, we also need to consider reforms of the procurement system.

Procurement reform is a basic component of an anticorruption strategy. It should be viewed as an opportunity to rethink *what* the government buys as well as *how* it goes about making purchases. Government purchasing specifications should take account of the risk of corruption. When possible, goods sold in international markets where benchmark prices exist should be favored over custom made or state-of-the-art products. Under decentralized systems, regional and local governments can favor goods and services sold in national market. In such cases, the state can look to private market prices as benchmarks and state its specifications in terms of standard off-the-shelf items (Kelman 1990, Rose-Ackerman 1978: 132-135).

Benchmarking can have an international dimension. Countries and subnational governments that are small relative to the markets in which they operate can make purchases of standard products in the international market. Market prices are excellent benchmarks here because the small government's own demand is unlikely to affect prices.

One way to obtain rough estimates is through data on United States trade. The Trade Research Institute calculates average prices and variances for goods using United States trade statistics and estimates the tax revenues lost to the United States from over-and under-invoicing (Pak and Zdanowicz 1994, 2002; Paul, Pak, Zdanowicz, and Curwen 1994). Because of product differentiation even within quite detailed categories, these price estimates are guesses, but they could give developing countries a starting point for negotiating with suppliers.

Benchmarking is in some tension with International Competitive Bidding (ICB) procedures whose sealed bidding process is often taken to be the presumptive standard of fairness and economic efficiency. The World Bank requires ICB, under which the lowest "evaluated" bidder must be accepted, for its infrastructure loans, and these standards have influenced the development of procurement codes worldwide.[16] The process does permit non-price factors to be weighed in the final decision but requires these factors to be specified and quantified if possible. It is appropriate for a project, such as a dam, that is capital intensive, self-contained, and uses known and tested technology. However, if followed mechanically, it can lead to low quality work and collusive bid rigging. Instead, for small aid-dependent countries, the reputation of bidders could be drawn from the international arena. An international organization might keep a roster of contractors with information on their past performance. To avoid controversy, however, such a system should focus on a few key variables that are measurable and comparable across countries. Relevant indicators might include evidence of fraud, corruption, cost overruns, and time delays. The World Bank could integrate such a roster into its revised Procurement Guidelines (1999) which state that the Bank will declare firms ineligible for Bank contracts "either indefinitely or for a stated period of time" if it determines that the firm has engaged in corrupt or fraudulent practices in connection with Bank-financed projects [Section 1.15(d)]. Thus one could imagine something similar to Golden and Picci's estimates for Italy although obviously these estimates would be less precise if applied internationally.

In correspondence with the author, Lucio Picci suggested an intriguing connection between benchmarking in public procurement and citizen oversight. He pointed to the way internet services, such as eBay, provide feedback on the reputation of buyers and sellers. The feedback is entirely voluntary and is a decentralized mechanism with broad reach. Although there are obvious risks, for example, a seller with a low reputation can reenter the system under a new name, and reputations can be influenced by self-interested buyers and sellers praising themselves (Dellarocas 2003).

Nevertheless, such a feedback mechanism might have applications to government contracting. Picci suggested that a benchmarking system organized by the central government in a country like Italy or internationally by the World Bank could provide information on the costs of various standardized infrastructure activities under different contracts. Citizens who use the services or observe the work being done could post opinions on the internet with respect to particular public works. There are obvious design problems that would have to be overcome to make such a system operational, but it seems worth study for countries with reasonably high levels of both literacy and internet access. It is not a viable option for the people at the bottom of the income ladder in some of the case studies outlined above.

Civil service reform can complement procurement reform by providing incentives to officials to perform effectively and avoid corruption. Bonuses earned by officials who achieve procurement goals could substitute for illegal payoffs. However, civil service reforms that simply raise wages to competitive levels are unlikely to be sufficient. One recent study, based on data from 35 countries, found that meritocratic recruitment was associated with measures of good bureaucratic performance, but that the role of competitive salaries was unclear (Rauch and Evans 2000). A study that examines the impact of a specific reform effort suggests a reason for the ambiguity. The study deals with a very narrow issue: hospital procurement of standardized supplies—saline solution, ethyl alcohol, iodine povidine, and hydrogen peroxide—by hospitals in Buenos Aires (Di Tella and Schargrodsky 2002). The authors studied the impact of a crackdown in which the central authorities checked the prices paid at 28 hospitals and used information of high relative prices as evidence that payoffs may have occurred. Prices decreased during the crackdown especially in the early months. Wage levels and enforcement intensity had complementary impacts except at high levels of enforcement where enforcement appeared to be a substitute for high wages. One cannot tell if these results generalize, but they do suggest that a policy of paying high wages to officials needs to be combined with a credible enforcement effort for optimal deterrence.

However, civil service reforms and enforcement against lower level officials are only necessary, not sufficient, for success in combating corruption in procurement. Scandals frequently have implicated top government leaders who profited from their inside knowledge and connections. The above proposals are not much help in dealing with such "grand corruption." They focus instead on middle level procurement decisions under the control of professional civil servants. They are, however, consistent with reforms that shift procurement decisions to career officials and tender boards. If rulers wish to insulate themselves from the demands of political supporters, they should create impartial bodies with independent procurement authority.

The basic reorientation of reforms efforts away from perfecting the bidding process toward making the overall purchasing environment more efficient and

effective is a fundamental shift in perspective spearheaded by Kelman's work (1990, 2002). It seems an especially valuable innovation for developing countries with limited capacity to carry out complex bidding procedures. Although competitive bidding sounds like a good idea, bidding does not play a rule in a truly competitive market. Instead, the market price is set through the multiple interactions of many buyers and sellers. The World Bank does permit what it calls "shopping" for off-the-shelf purchases so long multiple suppliers exist (World Bank 1999: section 3.5). My point is simply that countries should try to design their projects to favor shopping over sealed bidding as a way of limiting corruption.

Of course, frequently governments do need to make special purpose deals using a well-organized bidding process to minimize costs. Developing countries will be making large investments in special purpose infrastructure for years to come. These projects are unlikely to require sophisticated new technology, but they are one-of-a-kind. Thus the effectiveness of competitive bidding procedures will remain a central concern. Accepting the validity of the basic principles of International Competitive Bidding procedures for such projects, countries still need to assure robust competition among bidders. The same is true for competitive systems that make use of pre-screening processes. There are two problems—the possibility of collusion and the difficulty of attracting bidders. If contractors are willing to use violence to silence critics, the challenge to democratic state authority is greatest. The first order of business is then protection for whistleblowers and a willingness to follow up on allegations in a way that removes the impunity of officials. These procedures, however, must be designed to avoid encouraging people to use corruption scandals as a way to undermine one's political opponents.[17]

Developing countries could experiment with benchmarking, experience-rating for contractors, the adoption of more transparent processes, and civil service reform. In countries with a scarcity of skilled procurement experts and weak public accountability the case for bench marking and the purchase of standard items is strong. The cost\benefit calculus here requires a balance between reductions in flexibility and reductions in costs. The reduction in corruption is gained at the cost of a poorer fit between procurement specifications and the government's "needs."

C. Customs and Tax Administration

States cannot function if they are unable to collect taxes. A few countries rely heavily on outside grants and loans from international financial institutions, and a few still obtain considerable revenue from publicly owned enterprises. Most countries, however, require a functioning tax system. A legitimate democratic state appears to require that the state be able to collect taxes from its own citizens, not rely on outside sources of revenue. If citizens are not taxed, they have little incentive to hold the state accountable (Moore 1998). Many poor and emerging economies have very

low capacities to collect taxes from their own citizens and from businesses and tend to collect taxes in arbitrary and unfair ways. In nearly every developing or transitional country where diagnostic surveys have been conducted, customs and tax administration are cited as loci of frequent and large unofficial payments (Anderson, Kaufmann, and Recantini 2003: 10). One consequence of an arbitrary and corrupt revenue system is to drive firms to operate at least partly off the books. The 2002 BEEPS survey in Eastern Europe and the former Soviet Union found a negative association between the percent of sales reported to tax authorities and the proportion bribing tax authorities (Fries, Lysenko, Polanec 2003: 15). Dissatisfaction with the quality of public services becomes a justification for underpayment, and underpayment produces low quality services. [See Fjeldstad and Sembola's (2001: 2069) survey in Tanzania.] Thus limiting corruption in procurement and service provision can help limit tax avoidance. However, independent corrupt incentives exist in the collection of taxes and duties, and reduction in those incentives is the theme of this section.

Businesses and individuals frequently collude with tax collectors and customs agents to lower the sums collected and expedite services. As a result, revenue collection may be both inadequate and distributed unfairly. Taxpayers and corrupt officials divide the savings in taxes and duties. The costs are born by those taxpayers who are poorer and less well-connected and by the general public in the form of reduced services.

Take just a few examples. A major scandal in China revealed that state and party officials in a major port in southern China had been entirely corrupted by smugglers with a huge loss in customs revenue (Gong 2002). In Pakistan one study estimated that if the leakages caused by corruption and mismanagement could be reduced by fifty percent, the tax to GDP ratio would increase from 13.6 to over 15 percent (Burki 1997: 16). In Bolivia a highly politicized tax administration is also viewed a very corrupt and is estimated to lose millions in tax revenues through a mixture of corruption, smuggling and informal, off-the-book businesses (Kaufmann, Mastruzzi, and Zaveleta 2003: 355). A study of efforts to reform tax administration in Mexico and Argentina points to the costs of corruption and inefficiency in the revenue system as an underlying cause of the fiscal crises of the early 1980s. The weak and arbitrary aspects of the tax system in both countries contributed to a poorly functioning public sector and inefficiencies in the private sector as well. The resulting crisis persuaded political elites of the need for reform (Berensztein 1998).

The experience of a number of African countries illustrates the magnitude of the problem. In some studies the revenue shortfall was about 50% (Stasavage 1999: 71). In Gambia, in the early nineties, foregone revenue from customs duties and the income tax amounted to 8-9 percent of GDP (six to seven times the country's spending on health). Income tax evasion alone was 70 percent of revenue due. Only 40 percent of small and medium sized enterprises paid taxes, and many individuals

did not file returns. Underpayment of customs was facilitated by the lack of clear guidelines and of published tariffs. The extensive discretion of officials encouraged corrupt payoffs designed to evade tariffs. Of course, a well-working system would have been able to reduce tax and tariff rates, but the distortionary effect of such a high level of evasion is clear (Dia 1996: 46-47, 94-100). A study of tariff exemptions in Zambia, Tanzania and Mali estimated that exemptions, both justified and unjustified, produced a revenue shortfall of close to 50 percent (Low 1995). In Mozambique in 1995 the customs service collected 49 percent of the revenue it would have collected if no exemptions had been given. Officials added extra delays, overestimated the value of goods, and applied higher rates in an attempt to extract payoffs (Stasavage 1999). In Zaire, much of the country's output was smuggled out with the complicity of customs officials. Corruption was also pervasive in evading import duties and controls (MacGaffey 1991). Studies of the Gambia, Mozambique, and Ghana suggest that corruption permits the rich to avoid taxes (Dia 1996; Stasavage 1999). Tax avoidance in the Philippines reputedly means that the poor contribute twice as much as the rich, and 63 percent of imports pay no duty.[18]

Corruption in tax and customs is not just a transfer from one pocket to another. In addition, tax burdens are distributed unfairly, and resources are lost keeping the illegal behavior secret. A corrupt tax and customs system that favors some groups and individuals over others can destroy efforts to put a country on a sound fiscal basis and discredit reform. For example, in Mozambique interviews carried out in 1996 indicated that corruption had grown since the beginning of reform efforts in 1986. Overall taxes fell from 20 percent of GDP in 1993 to 17.6 percent in 1994 with import taxes falling from 5.1 percent to 3.9 percent of GDP (Stasavage 1999). Corruption is especially common when nominal tax rates are very high (De Melo, Ofer, and Sandler 1995; Webster and Charap 1993). High nominal tax rates lead to bribes and other types of tax avoidance which lead to even more avoidance, and so forth in a vicious spiral.

One response is to repeal certain taxes that are difficult to collect and to lower overall rates. Tax reform frequently involves simplifying taxes and levying them on bases that are difficult to hide or underestimate. For business taxes, presumptive taxes can be levied that are fixed independently of a firm's actual profitability. The reduction in corruption and tax evasion is traded off against the reduction in fairness. For example, Mexico introduced an alternative minimum tax of two percent on the real value of firm assets. A firm pays the maximum of the value of this tax and the corporate tax otherwise due. Small business pays a lump-sum tax per person employed, and medium-sized businesses are taxed on turnover. All these reforms raised additional revenue through reductions in tax evasion and in corruption (Das-Gupta and Mookherjee 1998: 311-312). Such reforms are, however, unlikely to be sufficient if officials have no incentive to work effectively and if the state does not

punish the underpayment of tax. For example, tax simplification in the Philippines apparently provided few benefits because there were no improvements in the incentives facing tax collectors and taxpayers (Das-Gupta and Mookherjee 1998: 410).

Reforms may produce a win\win situation where administrative costs are reduced because of tax simplification and revenue collections rise. Successful reform of a country's system of revenue collection should permit a reduction in nominal rates of tariffs and taxation. This may permit an escape from the trap where high rates lead to evasion, and evasion leads to higher nominal rates and even more evasion. A case study of India provides a classic case (Das-Gupta and Mookherjee 1998: 101-102). Despite an increase in rates, total revenue declined both because of an increase in corruption and a shift into off-the-books activity. In such cases, nothing short of a thoroughgoing reform of the structure and administration of the tax system will allow a breakthrough. Simply raising the wages of tax collectors and increasing surveillance are unlikely to be sufficient (ibid.). In contrast, Russia recently simplified its income tax system by introducing a flat 13% rate and introducing credible enforcement measures. Tax revenues have increased.

Incentive schemes have sometimes had positive effects. These can be incentives both for tax collectors and for tax payers. Das-Gupta and Mookherjee (1998: 257) report on efforts that combined the creation of a relatively autonomous bureaucracy with a budget linked, in part, to its success at collecting revenue. Reforms of revenue collection services in several African countries had similar features (Dia 1996). For example, Ghana in the eighties tried an enclave approach to tax and customs reform by creating a new National Revenue Service (NRS). Prior to the reform, tax revenues were 4.5 percent of GDP. Under the reform, the most corrupt existing officials were dismissed or retired. Pay and working conditions were improved. Increased salaries were accompanied by incentive systems to reward strong performance by individuals and by the agency as a whole. Revenue targets were established, and the NRS was given a bonus of 3.5 percent of tax revenue and 2.5 percent of customs revenue. Between 1984 and 1988 tax and customs revenue rose from 6.6 percent to 12.3 percent of GDP. Thus as long as the cost of the program did not exceed 5.7 percent of GDP, the program was a net revenue generator. The reforms illustrate the importance of combining improved base pay with incentives for good performance. Furthermore, rank and file officials must believe that corruption is rare at the senior levels. The program was a relative success, but it was not without problems. The rest of the civil service chafed at the special treatment afforded tax collectors. After all, the bonuses received by the NRS increased not only if effort increased, but also if taxes rose because of an exogenous increase in GDP. Furthermore, the Ministry of Finance objected to its loss of authority. In 1991 revenue collection was again placed under the authority of the Ministry of Finance although it retained some of its independence. Corruption reportedly increased (Chand and Moene 1999). The

strengths and weaknesses of several African experiments with Revenue Authorities are summarized by Devas, Delay, and Hubbard (2001).

In an instructive study of a failure, Fjeldstad (2002) analyzed an unsuccessful effort to reform the Tanzanian Revenue Authority along the same lines as the Ghana case. Before reform, lost revenues were high because of illegal behavior. Up to 70% of the value of imports did not appear in official statistics, and domestic businesses underreported production volumes and profits and falsified deductions. The reform focused on the control of discretionary tax exemptions, reform of the high and complex rate structures, improved pay and working conditions for tax officials, and strengthened enforcement. As in Ghana, a semi-autonomous agency was set up with local leaders of known integrity, and most staff were fired and had to reapply and take a test. The first year 1996-1997 was a seeming success with a 30% increase in revenue collected. However, between 1997 and 2001 corruption reemerged and revenue collection fell. The dismissed officials became "tax experts" who facilitated corrupt tax avoidance deals. Improved salaries did not deter officials. Fjeldstad points to the partial nature of reform. The tax system remained complex, non-transparent, and unclear.

One proposal is a contract with a private firm that both assesses and collects duties and then retains a fraction of the revenue collected. For example, Mozambique has experimented with such a system for customs revenues. In 1997 revenues jumped by 40 percent (Hubbard, Delay, and Devas 2001). Revenue collection has increased each year. In 2000 the contract was extended and is now set to expire at the end of 2004 (http://www.crownagents.com/). The contract is also meant to be a step toward a reformed and locally operated customs service, but that aspect of the project is behind schedule.[19]

Such contracts are expensive and are unlikely to provide a viable permanent solution. In the case of the customs service in Mozambique, the contractor obtains 3.5% of revenues collected but, in addition, Mozambique covered the costs of the expatriate staff. In 2003 there were 13 expatriate consultants and two short-term specialists. Overall the contract cost over 20% of projected revenues although net costs were presumably lower because the government saved money on its own bureaucracy (Hubbard, Delay, and Devas 2001). To see the implications of this fee, suppose that the reform doubles gross tax collections from $100 to $200. Of that, $160 is transferred to the treasury which, I assume, also saves $10 in collection costs for an overall revenue of $170, which is $80 above the old net revenue of $100-$10=$90. The increase in net revenue from $90 to $170 is an increase of almost 90%. Of course, these are just made-up numbers, but, in fact, gains do seem substantial in high corruption environments. Notice that in my example, if gross tax collections increased to $125 or less with no reduction in state expenses, contracting out would not be worthwhile. Low levels of corruption should simply be tolerated in that case unless inexpensive internal reforms are an option. Note that the size of

the bribes themselves does not figure into this calculation. The bribe is a transfer from the taxpayer or importer to the official. The social cost is the distortion introduced by the bribe in the form of reduced tax collections from bribe payers and a distorted incidence of taxes.

Durable reform should deal with the underlying incentives for tax evasion. In some countries the nominal level of taxes and duties is so high that citizens and businesses justify their evasion on the grounds that they cannot survive if they obey the law. In addition, tax laws are often complicated and unclear giving tax collectors leeway to make exceptions. These factors can produce a situation where a high proportion of households and businesses are law breakers. This gives the incumbent government a tool for controlling dissent and undermining political opponents. The goal should be a tax system with rates that can realistically be paid and with simple and clear standards. In addition, the rules must be transparent to the public, and systems of accountability must exist. If they do not, simple clear rules can simply permit a top ruler to extract payoffs more effectively. This is just one example of the importance of viewing reform in the context of the political-economic environment. Furthermore, governments can give taxpayers incentives to pay on time. The government of Mexico City, for example, is encouraging people to pay their taxes on time by giving them a discount if they file early.

Some reforms in the collection of state revenue are, in principle, costless. The goal is to reduce bureaucratic discretion, a policy that ought to both reduce bribes and reduce bureaucratic inputs. The problem is political will and the political power of those who pay and receive bribes. However, if personnel are deeply corrupt, simply changing the rules may not be sufficient. The state may need to replace officials, and new employees may need to earn higher salaries, have better working conditions, and get bonuses for good performance. Costly oversight and auditing may be necessary. One option is to contract out the collection of revenue to a private firm based in a developed country. This may increase revenue collection, but it is option and unlikely to be a feasible long term solution.

D. Business Regulation

A high proportion of firms surveyed in the Executive Opinion Survey in 2002 reported that the illicit purchase of laws, policies, and regulations was high/very high (see figure 8). These results appear to include both the outright purchase of general rules and corruption in the administration of existing policies. Bribery to obtain access to public utilities was also a prevalent in some regions. Corruption appears to take time. Data on Eastern Europe and the former Soviet Union indicate that the larger the share of firms that bribe public officials, the greater the proportion of senior managers' time spent dealing with public officials (Fries, Lysenko, and Polanec 2003: 16-17). The data indicate that corrupt firms usually spend more, not

less, time dealing with authorities. Figure 11 shows that in most countries in the region, corrupt firms average more time dealing with authorities than firms that report paying few or no bribes. This result suggests that corrupt systems are ones that create red tape and vague rules as spurs to the payment of bribes.

: FIGURE 11

Corruption occurs both at the time a business is established and later as it seeks to survive. The World Bank has pioneered studies of the hurdles facing those seeking to establish and maintain business firms throughout the world. One part of this research focuses on the costs in time and money of establishing a new business legally. Building on Hernando de Soto's (1989) research in Peru, these studies show how entrepreneurship is discouraged and how those who persevere are pushed into corrupt and off-the-books operations by the tediousness and expense of complying with the law. The second strand of research begins with measures of the shares of managers' and employers' time spent dealing with government officials. This research deals only with registered companies, but it, of course, indicates one reason why firms operate in the informal or "gray" economy seeking to avoid official notice.

A simple conclusion from this research is that firms would be much more productive if the government removed the rules and regulations that make entry and operation costly. This looks like a costless reform. Firm managers and employees redirect their time to productive activities, and more firms enter the market thus increasing competitive pressures and benefiting consumers with lower prices. Some of the studies of this phenomenon take this viewpoint, and see obstacles to firm entry and operation as pure costs. Unfortunately, this conclusion is too glib. Although reformers should examine the existing rules and regulations in most countries to determine if some can be eliminated, some business/government interactions can be socially beneficial. Then the proper response is not to eliminate the program but to reform it in ways that limits corrupt incentives. However, even with such reforms some costs will remain. I have already discussed two important examples in my discussions of tax collection and procurement and their reform. In addition, rules regulating environmental pollution, waste generation and disposal, worker health and safety, unionization, the issuance of securities, consumer fraud and product safety, and so forth have solid public policy justifications even if the details of a state's actual laws are far from ideal. Some countries may have such dysfunctional state institutions that it is better not to take on some regulatory tasks until conditions improve. Others, however, may be able to institute reforms that suit their level of capacity—similar to the simplified tax system discussed above.

This leads to a basic recommendation: Expand the diagnostic work already done to more countries but also include a more nuanced policy response that tries to sort out valuable from useless public programs. However, if reform is selective, the

result may simply give the remaining officials more power to extract bribes. It is quite possible that the actual level of payoffs might increase as the transaction cost of corruption fall. This can still be beneficial as less time is wasted by the firm and by public officials, but remaining corrupt officials still have an incentive to facilitate market monopolization to maximize rents. The "one-stop-shops", much touted by development agencies, may simply be efficient bribe-collection agencies. Thus, in streamlining business/government relations, governments need to decide what public functions are really necessary and then construct bureaucratic procedures that limit corrupt opportunities through such devices as impersonal procedures; simple, transparent rules; inter-bureaucrat competition, effective complaints and appeals procedures; etc. (Rose-Ackerman 1999: 39-68, 146-149).

There appear to be some win\win possibilities here where dysfunctional rules and regulations can simply be repealed. The main cost is an expansion of the diagnostic work already being done by such organizations as the World Bank to include more countries and a modification of existing work to highlight the benefits of government programs that impose financial and time costs on business.

E. International Efforts

Multinational firms are involved in many deals with developing countries and emerging economies. If corruption is involved, the result may bring few benefits to the host country and impose costs on the multinational. This has led to international treaties to control corruption – most notably at the Organization for Economic Cooperation and Development (OECD), the Organization for American States, the Council of Europe, and, most recently, the United Nations. These documents all reflect the salience of the issue of global corruption, but none of them is very powerful as a law enforcement tool.

Their impact will depend upon their ability to change the discourse inside member countries and in the international business communities in ways that also change behavior. These treaties have so far not had much concrete impact although they do seem to have changed the dialogue over corruption in ways that have a real impact on firms that care about their reputations. However, to go further, these treaties will have an impact only when combined with strong domestic efforts in both home and host countries. I will not describe these efforts here. Those with a deeper interest in the current status of these treaties can consult the relevant websites maintained by each organization.[20] I discuss several possibilities that are related to current debates and to some aspects of these international agreements. My main focus is on alternative forms of information disclosure and accountability in extractive industries. I conclude with a discussion of asset recovery initiatives.

Extractive industries (e.g. oil, minerals) are a current focus because considerable empirical evidence suggests that, when the state is weak or venal, there can be

a resource curse in which the presence of such resources hurts economic growth by diverting energy into rent-seeking instead of productive activity (Rose-Ackerman 1999: 213-215). Paul Collier and Anke Hoeffler (2004) point the link between natural resource dependence and civil war. The management of such resources is of great importance especially in Sub-Saharan Africa which is on the verge of an oil boom and has many other poor resource-dependent countries. According to *The Economist*, "a handful of states are expected to receive $200 billion in the next decade" as a result of oil and gas exploitation (December 6, 2003, p. 39).

One initiative is a campaign backed by a coalition of nongovernmental and civil society organizations called "Publish What You Pay." The campaign's goal is an international regime that requires disclosure of net taxes, fees, royalties and other payments made by natural resource companies to developing country governments. The aim is to help citizens of these countries hold their governments responsible for the use of revenues from these investments (http://www.publishwhtatyoupay.org). Of course, if the country's government is not dependent on the support of its own citizens, this can be an empty gesture that simply informs helpless citizens that their rulers are benefiting at their expense.

The second proposal is an international, multi-stakeholder effort called the Extractive Industries Transparency Initiative (EITI). The EITI includes host countries in the mix and seeks to have both sides of the transactions make public reports of legal payments. Part of the motivation for this initiative is to permit outsiders to check if there is any discrepancy between the figures reported by firms and by governments. At this point the EITI is working toward a voluntary pilot program involving a few resource dependent countries. The pilot countries are likely to be drawn from the following list: East Timor, Azerbaijan, Ghana, Trinidad and Tobago, Democratic Republic of the Congo, Indonesia and Nigeria. One idea is to use a "trusted third party", perhaps the World Bank, to develop a standardized process and to receive reports (details and updates at http://www.dfid.gov.uk). As a background report prepared for a February 2003 meeting makes clear, there are a number of problems in making the data comparable and in dealing with contracting issues, including confidentiality. Furthermore, presumably a program could go forward only if all the multinational and domestic contractors and concessionaires in an industry agree on the procedure. Thus even a "voluntary" procedure would have to have mandatory aspect as participating countries make disclosure a condition for doing business. Collier and Hoeffler (2004) discuss EITI in their Copenhagen Challenge paper as a promising option to reduce the risk of civil conflict and to fuel growth. They estimate the total discounted present value of benefits at roughly $29 billion with trivial costs. Even if those benefit numbers are much overstated, the potential net gains look large is absolute number although they are a very small share of the discounted present value of world income.[21] The main problems are the

difficulty of specifying exactly what EITI requires and of being sure that its terms are followed. This is one example of a program with small social costs but that will impose massive losses on those in favorable positions to extract rents. Thus it will not be easy to implement.

Third are efforts that concern host country use of the funds from oil and mineral extraction. For example, the World Bank, which helped finance the Chad/Cameroon pipeline, has set up an International Advisory Group to make periodic reports on institutional capacity of Chad and Cameroon and on the ways funds are being used (http://www.gic-iag.org). The Bank also required Chad to set up an independent watchdog Revenue Oversight Committee to scrutinize how the oil money is spent. The Committee has rejected over half of the government contracts and insisted on open bidding. However, it has some weaknesses of its own with low staffing levels and tight deadlines that limit oversight (*The Economist* December 6, 2003, p. 39). The World Bank has made this project a test case in the effort to be sure that natural resource revenues benefit a nation's citizens. Its successes and failures are worth monitoring as project revenues begin flowing in.[22] However, making natural resource payments from multinationals contingent on a country's own institutional oversight is only possible in very poor, aid dependent countries such as Chad. Other countries can simply refuse to accept loans from international financial institutions.

Nevertheless, these efforts seem worth pursuing. The initiatives are related to the OECD Treaty outlawing overseas bribery. Multinationals may hope that by supporting greater transparency, they can avoid having payments that they record as royalties or taxes end up in the personal bank accounts of leaders. They may also hope that transparency will limit the financial demands of host country officials. However, the leaders of countries that have only weak democratic institutions may not be deterred by transparency, which, although necessary for corruption control and good governance, is not sufficient. If civil society is weakly organized in the host country and lacks the expertise to understand company and country reports, transparency may have little impact inside the country. Its main role may be in putting international pressure on both firms and country leaders. This suggests that the NGOs behind the "Publish What You Pay" initiative have a point is pushing for a mandatory disclosure system managed by an international organization. The mandatory aspect of such a plan could take the form of making such disclosure by firms and governments a condition for receiving favorable investment guarantees and subsidies from home countries or from the international aid and lending organizations such as the World Bank Group, including the IFC and MIGA.

The international business community is beginning to recognize the costs of corruption to the global investment environment. Insofar as this is true, it suggests that international businesses themselves could contribute to the effort by providing funds and technical assistance to countries interested in reform. This is already being

done through professional associations such as the American Bar Association, but the aid and lending organizations might explore the possibility of collaborative projects. For example, one aspect of the EITI is a plan to provide technical assistance to developing countries to improve their public budgeting procedures and reports. Such assistance could be underwritten by the firms that invest in the countries in question although, of course, they ought not play a direct role in the administration of such programs.

Although a wide range of options have been proposed to deal with corruption at the international level (Rose-Ackerman 1999: 177-197), I conclude with just one additional possibility, asset recovery—an important part of the new United Nations treaty. One key requirement is to make corruption a predicate offense to the application of money laundering requirements. This broadening of the definition was included in the United States Patriot Act in 2001, but it is not a universal provision of such laws. A second issue is the grounds under which assets can be frozen and ultimately turned over to the government of the country of the corrupt official. The process is often cumbersome if it works at all. Thus the Congo has had little success in retrieving Mobutu's overseas riches, and Nigeria has only recently obtained substantial sums from overseas banks that hold funds deposited their by Sami Abacha, its former ruler. Kenya's new government has decided not to prosecute its former president, in part, because of the difficulty of recovering assets.[23] Enhanced asset recovery appears to depend not so much on a willingness to bear large costs as on changes in entrenched legal regimes that would require a difficult and controversial rethinking of present practices

III. Options for Improving Governance and Reducing Corruption

The operation of the state and its interaction with the public are key challenges facing the world. If government performance does not improve in many states, programs designed to help the poor, improve the natural environment, and stimulate economic growth will have little impact and risk inflicting harm.

Estimating the costs and benefits of specific reforms is difficult even if cross-country research indicates that the gains from reducing corruption and improving governance are large. The main problem is tracing specific links from particular, concrete policies to desirable outcomes. Even the World Bank, which has been a leader in quantifying the costs of the corruption, has been unwilling to organize the data in that fashion. However, some options are almost costless. Hence, even if the benefits cannot be precisely measured, the rates of return are large. This is, of course, not to say that there are no losers. Obviously, individuals and firms, many with political power, benefit from the status quo and will oppose change. A major challenge for governance reform is to overcome or co-opt entrenched interests.

Unresolved empirical issues limit the estimates of the relative cost-effectiveness of different strategies and the ways in which distinct alternatives interact. Thus an option may be better than the status quo but not necessarily better than another proposed reform. Furthermore, some of the options have never been tried on a large scale and have never been subject to systematic efforts to measure their effectiveness. Thus, reformers need to design experiments and pilot programs to test the value of options that appear promising. Based on my collection of reform options, there are several promising options.

Option 1: Grassroots monitoring and service delivery with technical assistance and information provision provided centrally by government or nongovernmental organizations. Benefits: Cost savings on existing programs that have ranged as high as 400%. Better overall economic performance and access of the poor to public services. Costs: Opportunity cost of people's time; costs of consultants and central government officials to help design programs and provide information. Demoralization costs if government does not respond to citizen complaints Note: Assuming the underlying program is beneficial, net benefits for successful programs are likely to be large with large benefit/cost ratios, but more needs to be learned about what works and is sustainable. Positive model cases: Brazilian urban democracy, monitoring of Uganda school funding, Nepalese local public works, South Africa Community Participation Programs.

Option 2: Procurement reform: Develop benchmarks and use them to reward efficient providers of public services. Consider integrating benchmarking with web-based reputation system based on public input. Role for international institutions, regional bodies, or central governments in providing benchmarking cost estimates and setting up interactive public comment systems. Encourage competition in providing goods and services to the state through use of more open procedures. More purchase of standardized products sold in international markets. Benefits: Cost saving on public contracts that may total 30-40% according to some estimates.

Costs: Costs of gathering benchmarking information and creating a system to use it. Note: Once again, assuming the underlying project is worthwhile, net benefits and B/C ratios will be large with benefits many multiples of costs. The main problem is a "technical" one—no one really knows exactly how to design a viable system. Model Cases: Golden and Picci's work on Italy, Pak and Zdanowicz's estimates of over-and under-invoicing in US, United States procurement reforms in the 1990s spearheaded by Kelman.

Option 3: Reform of revenue collection through tax simplification, incentives to collectors and tax payers, monitoring. Short-term use of private firms from outside

the country to assure integrity. Benefits: Increased revenue collection in the best cases was close to 100%. Costs: Increased pay and bonuses for collectors or fees paid to outside contractors, but these seldom total more than 50% of the revenue collected. Because the costs apply to all revenue, the existing situation must be quite dire to justify these expenses. But the costs and revenue gains can be checked ex post so the policy is self-correcting. A further cost is demoralization costs imposed on other government employees who see the benefits flowing to the tax office. Note: Net benefits and B/C will be high in many cases. Either the state can lower taxes or raise the level of service provision, but either way the productivity of public spending rises. Negative model: Tanzania. Mostly positive models: Ghana, Mozambique.

Option 4: Reduction in the state-imposed costs of establishing a new business and in the costs associated with ongoing business\government relations. Regulatory cutbacks tempered with concerns for valid goals of some public regulations. Benefits: Encourages formation of new businesses and increases economic value of existing businesses. Less managerial time spent dealing with public officials. Costs: Close to zero for pure "red tape," but reformers also need to evaluate any benefits forgone from programs with some social value. Note: If reforms are designed with care, there are very high B/C ratios and net benefits.

Option 5: International Options: Technical assistance to develop monitoring and transparency initiatives as in the Chad/Cameroon pipeline and the Extractive Industries Transparency Initiative. Enhanced asset recovery. Benefits: More of the benefits of extractive industry projects would flow to developing countries. Given the leakage in some past projects, this could increase host countries' benefits substantially. Increased risk of asset recovery could reduce the incentives to engage in corruption. These are transfer or pecuniary benefits that shift resources from multinationals and key political insiders to ordinary citizens in poor countries. However, research on the costs of corruption suggest that there are also efficiency gains as well. For example, Collier and Hoeffler (2004) estimate that the total discounted present value of a successful EITI initiative could be $29 billion.

Costs: Administrative costs of setting up such systems which should be only a few percentage points of the value of any project. Note: Although the net benefits of EITI appear large, some technical issues have not been resolved so this is not an "off-the-shelf" option. A range of experiments could be carried out in this area involving pilot programs in vulnerable countries.

I conclude with a few thoughts about the relationship between these policy proposals and the international environment. Consider aid and lending. Presently there is an ongoing debate about the value of conditionality in the provision of aid.

"Conditionality" in some broad sense is inevitable. International donors must choose where to put scarce funds, and they will consider where the funds will have some positive payoff. A weak state or one with high levels of corruption will be unlikely to manage aid well and so will get less. A state that does receive aid must comply with financial reporting requirements to assure that the funds are not lost to corruption and waste. Such conditionality, however, is less directly intrusive than aid that comes with explicit requirements for institutional reform. This latter type of conditionality has not been notably successful. An alternative is to organize projects that are directly focused on improved governance. For example, the Chad Revenue Oversight Committee and International Advisory Group for the Chad/Cameroon pipeline are cases in point that deserve to be carefully studied to isolate their strength and weaknesses.

I have documented some successes and some failures, but projects that improve governance and oversight seem the place to put external resources so long as a plausible exit strategy can be designed so that external funds and experts can leave with some assurance that a program will continue. A condition of such projects should be a research component that measures progress (or its opposite) by providing information on background conditions, tracking the design and implementation of the reform, and measuring outputs. Donors and country partners would try to quantify inputs and outputs in terms such as the speed and effectiveness of government activities, the satisfaction of citizens, and the distribution of benefits. Sometimes, as in a tax or procurement reform, the benefits can be quantified in terms of additional dollars collected or cost savings, but in other cases, such as more transparent government, the benefits take the form of greater citizen satisfaction and better government accountability. These factors are valuable in their own right and are associated with higher levels of growth and individual well-being, but the precise links from specific policy interventions to outcomes are not well-specified.

Recent discussions of how to allocate foreign assistance to developing countries sometimes conclude that some countries have such poorly functioning institutions that no external aid should be provided because so much of it will be lost. This represents not, as some say, an end to conditionality but is instead conditionality writ large—at the level of the country as a whole, rather than at the level of the program. The best mixture seems to be broad-based decisions about which countries to support with some share of aid taking the form of grants to improve government performance. Outsiders would not micromanage individual projects, for example, to build roads, support education, provide health care. Instead, they would supply technical assistance that could lead to a quite deep involvement with the details of government operations. In contrast, policies which try to isolate corrupt countries and individuals from the international community encourage their rulers to descend into paranoia and isolation and are ineffective ways to help the citizens of these

countries who are the real victims of corruption. Real reform requires systemic policy initiatives. Corruption is a problem of institutional failure. A "clean hands" policy in which wealthy countries hold themselves aloof from tainted countries and individuals without doing anything actually to address the underlying problems will simply further divide the world into rich and poor blocs.

NOTES

1 Henry R. Luce Professor of Law and Political Science, Yale University. I am grateful to Madiha Afzal and Dionysia-Theodora Avgerinopoulou for very useful research help. In parts of this paper I draw on Rose-Ackerman (1999). I am grateful to Daniel Kaufmann, David Nussbaum, Luccio Picci, Martin Raiser, annd Jong-Song You for helpful comments and current references.

2 Correspondence with Daniel Kaufmann, World Bank Institute, February 2004. The World Bank Institute is preparing a document explaining the derivation of this figure and considering the relationship between the volume of bribes and the social costs of bribery.

3 Kaufman (2003, Annex 2, figures 1A, 1B, IC) presents three figures showing the postive correlations between the log of read GDP per capita and corruption, the rule of law, and voice and accountability, respectively. The governance measures are derived from survey evidence mostly based on the perceptions of business people and country experts.

4 The corruption measure is an ordinal index derived from surveys, not a cardinal measure. Thus, a move from 2 to 3 on the index might imply a greater increase in integrity on some cardinal measure, such as level of bribes per capita, compared with a move from 8 to 9. One should not give a cardinal interpretation to indices of corruption. If a country's index fall from 6 to 3, this does not mean that corruption has been halved. However, if one compares countries at any CPI score between 2 and 4 with those between 8 and 9, there is a greater spread in the HDI levels in the former case than in the latter. There is, however, another aspect of the data that deserves mention because it determines the curvilinear shape in figure 1 The HDI uses a logarithmic scale for the income portion of the index, a technique the compresses the scale for wealthy countries. A similar graph with per capita income on the y-axis instead of the HDI shows a more dispersed pattern of income at higher levels of the (somewhat different) corruption index (Kaufmann 2003, figure 1A). However, at low levels of the index (that is, in highly corrupt environments) the data points continue to appear more dispersed than at high levels.

5 Neither predictability of bribe requests nor positive views of government on other questions (a "kvetch" effect) affected that conclusion and no measure of these effects was significant (Kaufmann, Mastruzzi, and Zavaleta 2003: 372-377).

6 Batra, Kaufmann, and Stone (2003: 14). The survey results were converted to binary zero/one codings with zero indicating the desirable outcome for business (ibid.: 11). A related study by Fries, Lysenko, and Polanec (2003: 40) using only data from Eastern Europe and the Former Soviet Union produced similar results. Qualitative perceptions of corruption, crime, judicial quality, regulatory constraints, taxes, and financing constraints significantly affected GDP per capita in 2001, real GDP growth from 1997-2001 and real GDP growth in 2002, all in the expected direction.

7 Entrepreneurs with the least secure property rights invest 40% less than those with the most secure property rights. At the time of the survey in 1997, the absence of bank finance did not prevent firms from investing because they were profitable enough to satisfy their investment needs internally (Johnson, McMillan, and Woodruff 2002). Although employment growth is unrelated to property rights, high sales growth is significantly associated with more secure property rights (Johnson, McMillan, and Woodruff 2000).

8 See also Graf Lambsdorff (2003a) who concludes, using cross-country data, that legal reform, directed at the improvement of property rights and the maintenance of law and order, is crucial for attracting foreign capital.

9 Fjeldstad (2003) provides a literature review on decentralization and corruption that cites studies that contradict the results for federalism found in the sources listed in the text. In any case, it is important to distinguish between federalism and explicit policies designed to empower those at the grassroots. I discuss the latter below.

10 Of course, Suharto did actually resign from office in May 1998, but as Fisman points out, this is a difficult event to study within his framework because so many other things were happening at the same time: the "event window" was several months long, the successor was a Suharto ally, and trading volumes were exceptionally low by the end of 1997. Perhaps for these reasons, the relationship did not hold in the beginning of 1998 except for steep declines in the shares of firms controlled by Suharto's children. (Fisman 2001: 1100, note 9).

11 See, for example, table 2 in La Porta et al.(1999: 240-241). High levels of corruption are highly correlated with bureaucratic delays and low levels of tax compliance on a country by country basis.

12 For an excellent collection of articles that focus specifically on failed states see Rotberg (2003, 2004). For more on the establishment of the rule of law in weak states see Rose-Ackerman (2004) in one of Rotberg's volumes.

13 Transparency International issues a cross-country index of corruption that is a compilation of others' rankings based moatly on perceptions of the level of corruption in business dealings. New Zealand and Singapore are near the top of the list along with the Scandinavian countries, Canada Australia, and the Netherlands. The 2003 Transparency International Corruption Perception Index is available at *http://www.transparency.org/surveys/index.html#cpi*. The United States Department of Justice (DOJ) prosecutes cases of corruption at all levels of government. Over the decade 1993-2002, the DOJ obtiained 20, 497 convictions (9.821 of federal officials, 5,782 of state and local officials, and 4,894 of private citizens involved in public corrption offenses) (United State Department of Justic, 2003). Obviously some convictions were associated with the same underlying corrupt practices.

14 See Tanzi and Davoodi (2002a) for a review of empirical work on corruption, growth and public finance. A study of structural adjustment lending in seven African countries concluded that much investment spending was of dubious worth. "'White elephant' projects, inflated contracts, flight capital, and other associated ills became rampant before —and eventually contributed to —the [government fiscal] crisis in each case. A major aim of adjustment programs has been to weed out these undesirable investments (particularly in the public sector) and to improve overall efficiency (Faruqee and Husain 1994: 6)."

15 For more details see Golden and Picci (2002) who report that the overall index of physical capital is not very sensitive to the method of aggregation.

16 See World Bank (1999: 25-28) at *http://web.worldbank.org/WBSITE/EXTERNAL/PROJECTS/PROCUREMENT/0,,contentMDK:20060840~pagePK:84269~piPK:60001558~theSitePK:84266,00.html*. The World Trade Organization's (WTO) Agreement on Government Procurement and related documents are available at *http://www.wto.org*.

17 As an example, see "Treacherous Roads," *The Economist* December 20, 2003, p. 56. The article reports on the murder of a young engineer employed by the state of Bihar in India to manage part of a highway project. He sent a letter to the Indian Prime Minister outlining a list of "dodgy practices". The letter was leaked to the relevant contractors, and the engineer then received threats. The authorities did not respond, and the engineer was eventually shot and killed.

18 *Far Eastern Economic Review* April 20, 1996.

19 For example, a 2002 report pointed to problems in achieving this goal. See *http://www.u4.no/projects/projects.cfm?id=103*.

20 OECD Convention on Combating Bribery of Foreign Public Officials in International Business Transactions, December11,1997, *http://www.oecd.org/document/21/0,2340,en_2649_34859_2017813_1_1_1_1,00.html*. Council of Europe, Criminal Law Convention on Corruption, Jan uary 27, 1999, E. T. S. 173 (entered into force 2002), *http://conventions.coe.int/Treaty/EN/Treaties/Html/173.htm* and *http://www.greco.coe.int/docs/ResCM(1999)5E.htm*,

Inter-American Convention Against Corruption, March 29, 1996, 35 I.L. M. 724 (entered into force March 6, 1997, available at *http://www.oas.org/main*. United Nations Convention Against Corruption, Dcember 9, 2003, available at *http://www.unodc.org/unodc/crime_convention_corruption.html*.

21 World income in 2002 was $32.2 trillion. Even supposing no growth in the total, the discounted present value of a 10 year stream at this level, discounted at 5% is $248.6 trillion. The estimated benefits of EITI are .012 per cent of that total.

22 "Greasing the Engines of Change in Chad," *The New York Times*, February 18, 2004.

23 "Kenya Joins Nations Pursuing Funds Stolen by Ex-Leaders," *New York Times*, December 21, 2003.

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Susan Rose-Ackerman

Henry R. Luce Professor of Jurisprudence,
Law School and Political Science at Yale University

GRÁFICOS E TABELAS

FIGURE 1: HUMAN DEVELOPMENT INDEX AND CORRUPTION PERCEPTIONS INDEX
Source: Calculated from UNDP and Transparency International data.

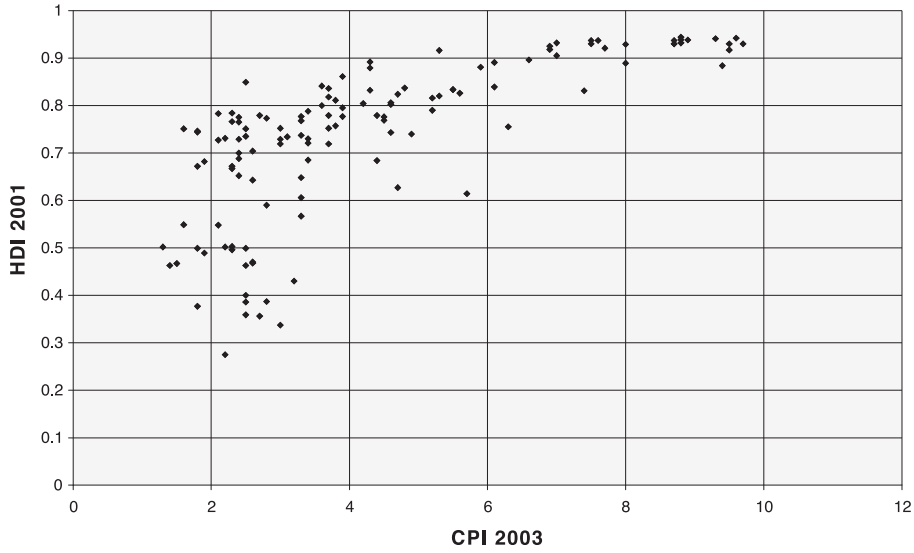
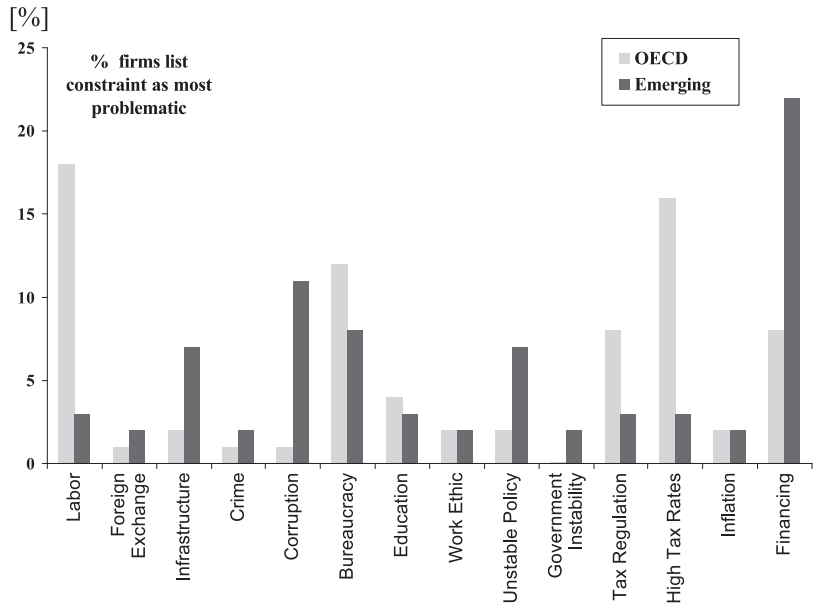


FIGURE 2: KEY BUSINESS ENVIRONMENT CONSTRAINT TO THE FIRM: EMERGING ECONOMIES AND OECD
SOURCE: KAUFMANN (2004)



Source: Executive Opinion Survey 2003. Question 13.01.
From the following list, please select the five most problematic factors for doing business in your country, and rank them between 1 (most problematic) and 5. The figure shows the percent of firms ranking the said constraint as the most problematic among the 14 items on the list.

TABLE 1: CITIZENS' FEELINGS ABOUT GIVING MONEY OR A PRESENT
SOURCE: MILLER, GRODELAND, AND KOSHECHKINA (1998, TABLE 23)

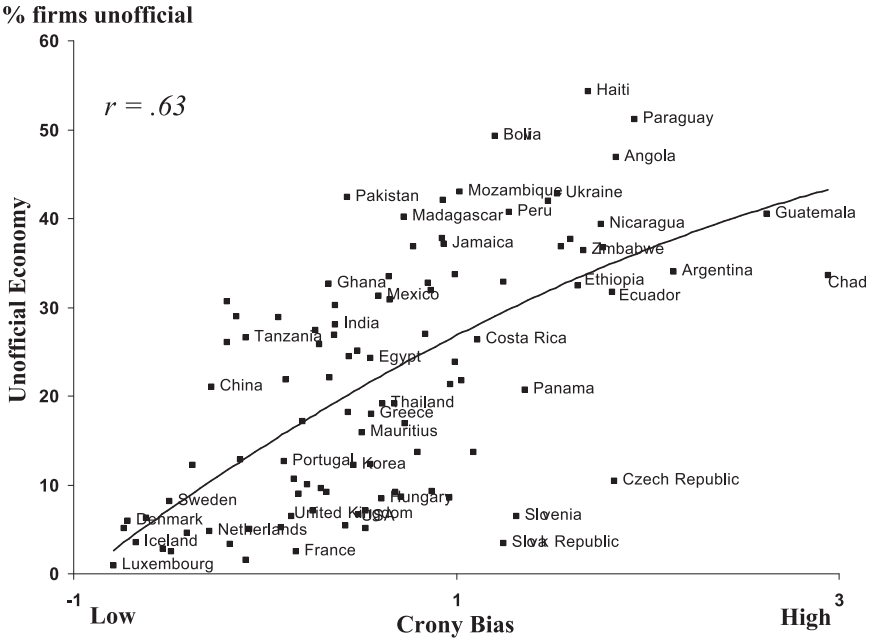
Q103: Suppose people gave money or a present to an official and got what they wanted, would they be most likely to feel…

Q104: But if they thought very few other people gave such things to officials, would they then be most likely to feel…

	Czech Republic		**Slovakia**		**Bulgaria**		**Ukraine**	
	Q 103 %	Q 104 %	Q 103 %	Q 104 %	Q 103 %	Q 104 %	Q 103 %	Q 104 %
happy	50	15	63	18	66	36	55	22
angry	25	36	23	37	13	20	11	24
worried	7	15	5	14	11	16	18	34
ashamed	18	34	8	31	11	29	16	20

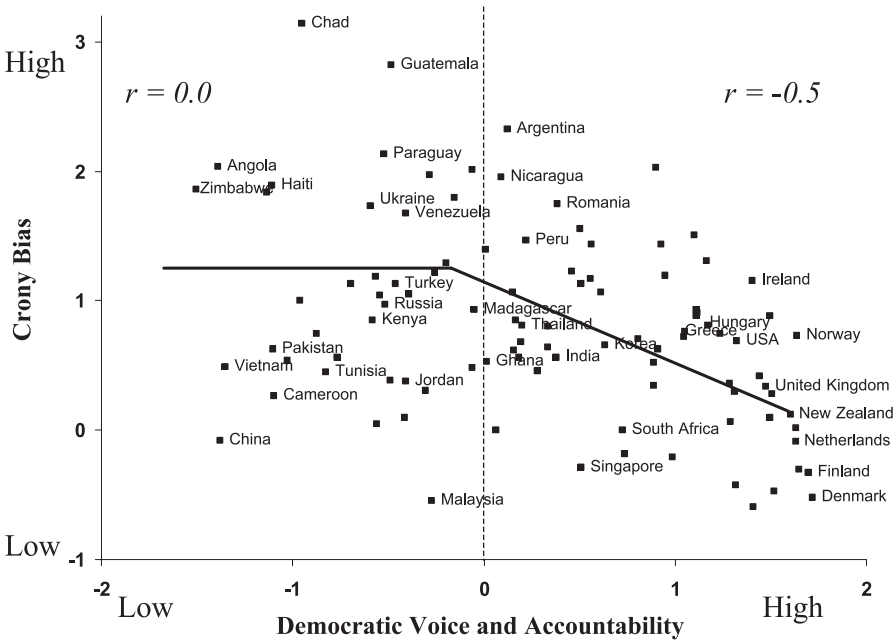
Note: 'don't know', 'mixed/depends' etc. answers were recorded if given spontaneously, but never prompted; they have been excluded from the calculation of percentages.

FIGURE 3: THE UNOFFICIAL ECONOMY AND CRONY BIAS (DATA FROM WORLDWIDE SURVEY, 2003)
SOURCE: KAUFMANN (2004)



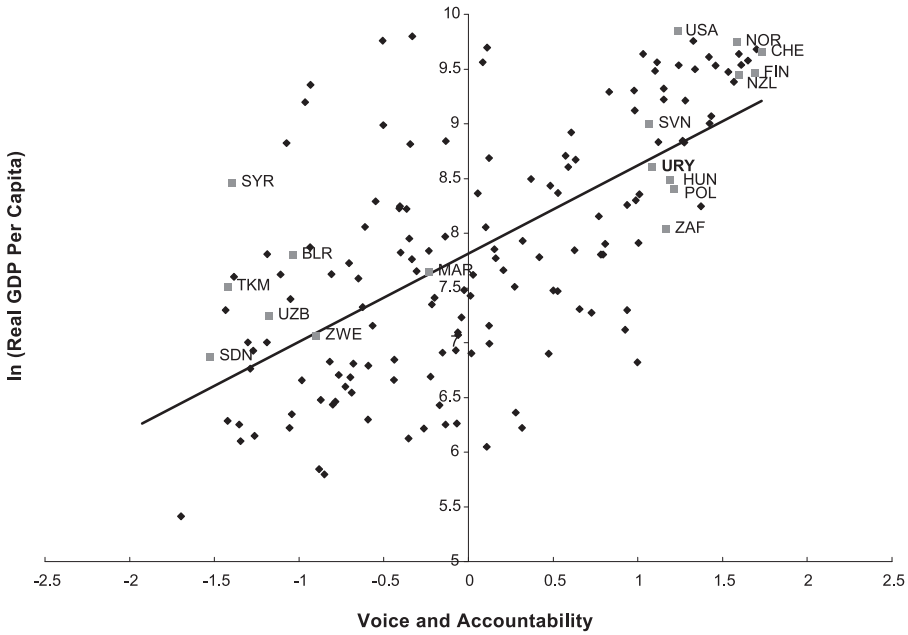
Note: Only selected countries among the 102 are labeled due to space limitations. Unofficial economy data drawn from firms' responses to following question: What percentage of business in your country would you guess are unofficial or unregistered? (categorical, converted using minimum within each range). Crony bias is constructed by authors, based on data from the 2003 Survey of firms in 102 countries, calculated as the difference between influence by firms with political ties and influence by the firm's own business association.

FIGURE 4: CRONY BIAS AND VOICE AND ACCOUNTABILITY
SOURCE: KAUFMANN (2004)



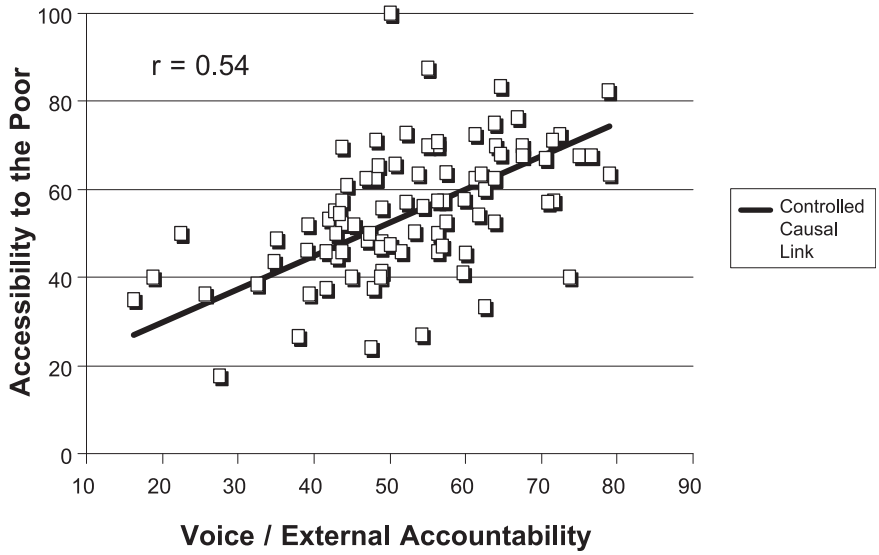
Crony bias defined in note of Figure 5 and text. Voice and accountability variable from Kaufmann, Kraay, and Mastruzzi (2003).

FIGURE 5: VOICE AND ACCOUNTABILITY AND PER CAPITA INCOMES
SOURCE: KAUFMANN (2003)



Notes: This figure plots a measure of voice and accountability in 2000/01 (on the horizontal axis) against real per capita GDP in 1995 (on the vertical axis). The governance ratings on the vertical axis are based on subjective assessments from a variety of sources, are subject to substantial margins of error, and in no way reflect the official view of the World Bank, its Executive Directors, or the countries they represent.

FIGURE 6: EXTERNAL ACCOUNTABILITY/FEEDBACK IMPROVE ACCESS OF THE POOR TO PUBLIC SERVICES (BOLIVIA GAC DIAGNOSTIC)
SOURCE: KAUFMANN (2003)



The sample of institutions includes 44 national, departmental, and municipal agencies that provide services to the poor. Each point depicts an institution.

FIGURE 7: UNBUNDLING CORRUPTION - EXECUTIVE OPINION SURVEY (GCR) REGIONAL AVERAGES, 2002
SOURCE: KAUFMANN (2003)

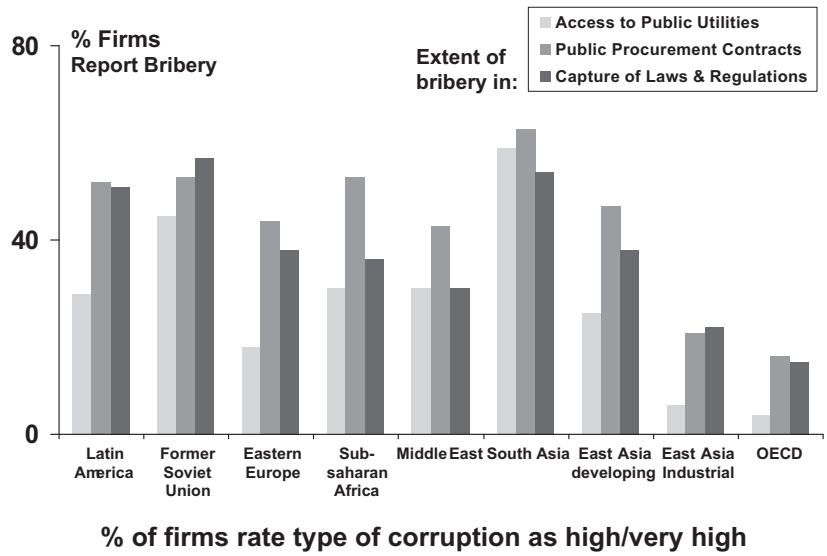


FIGURE 8: MAP OF PROPOSED LEVEL OF CORRUPTION BY REGION, C.1997.
SOURCE: GOLDEN AND PICCI (2004)

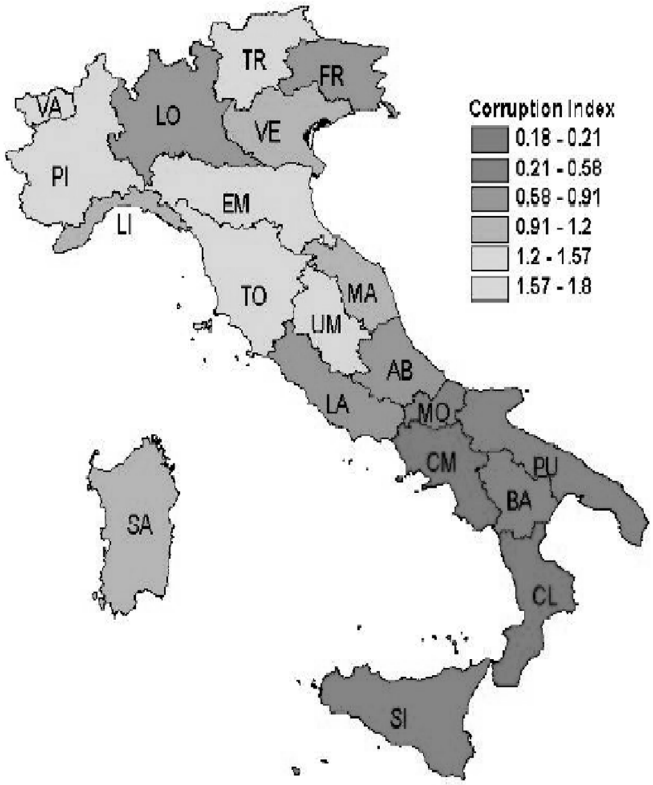


FIGURE 9: CORRUPTION AND PER CAPITA INCOME - ITALY
SOURCE: GOLDEN AND PICCI (2004)

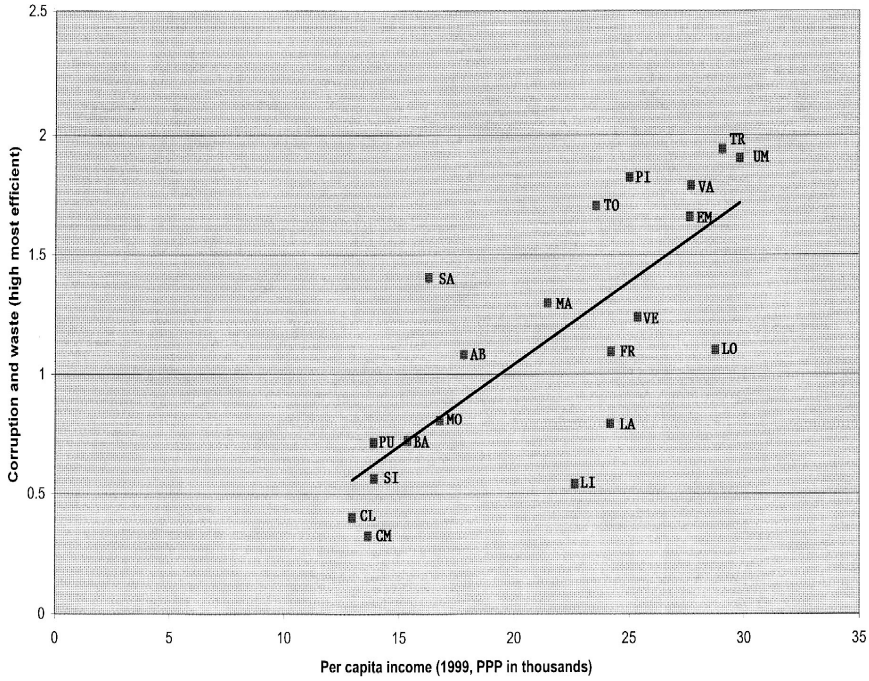
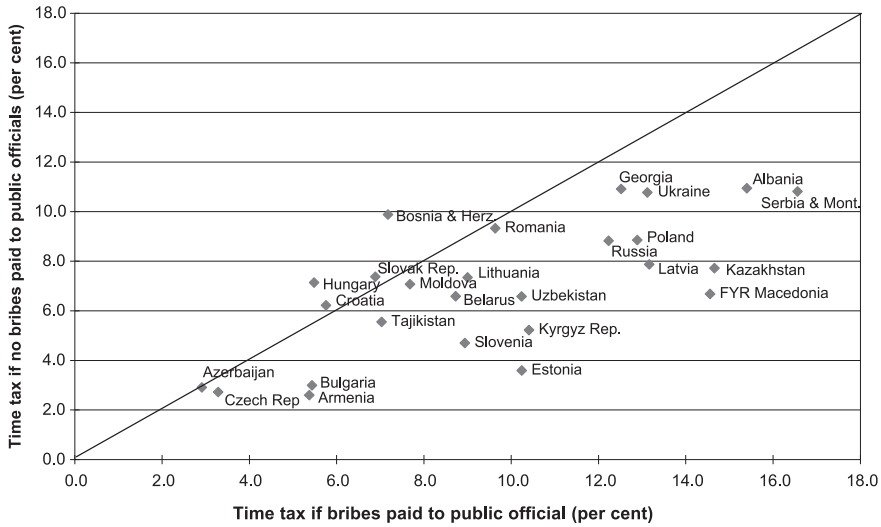


FIGURE 10: AVERAGE TIME TAX FOR FIRMS PAYING BRIBES TO PUBLIC OFFICIALS AND FOR FIRMS NOT PAYING BRIBES, BY COUNTRY
SOURCE: GOLDEN AND PICCI (2004)



Note:
1) Time tax is calculated for each country as an unweighted average of individual firms' responses on the proportion of senior managements' working time spent dealing with public officials. The averages are calculated separately for those firms that bribe frequently or more to deal with public officials in areas of business regulation and those that do not.

FROM THE DEVELOPMENTAL TO THE REGULATORY STATE: THE TRANSFORMATION OF THE GOVERNMENT'S IMPACT ON THE BRAZILIAN ECONOMY.

Edmund Amann[1] *and Werner Baer*[2]

Brazil's large-scale privatisation programme in the 1990s presents the image of an economy in transition from state domination to one in which market forces prevail. The aim of this article is to show that such a characterisation of events masks a far more nuanced and complex picture in which the withering away of the state has been more apparent than real. Moreover, with the election of President Lula da Silva in October 2002, a profound shift in policy has occurred which beckons a resurgence of intervention and a recasting of the regulatory role of the state. To advance our argument, we shall mainly focus on the experience of the public utilities sector, in particular charting its experiences following privatisation.

To begin with, however, we set matters in a broader context briefly reviewing the evolution of state participation in the economy in the period stretching from the 1930s to the late 1970s, stressing its influence in shaping the industrialisation process. In addition, we shall review the transformation of state enterprises from being a mainly positive influence on the Brazilian economy to becoming increasing dysfunctional. This will be followed by a brief overview of the extent of the privatisation process of the 1990s, and the resulting change of the role of the state in the country's economy, that is, from being a direct participant to being mainly a regulatory agent. Our particular concern in this regard will be to offer a preliminary assessment of the success of the state's new "regulatory approach" focusing on the experiences of the electricity and telecommunications sectors. The paper concludes by examining the likely development of utilities regulation now that President Lula da Silva's government is in place.

The participant state: 1930-1980

Beginning in the 1930s and accelerating in the post World War II period the state enterprise sector became dominant in public utilities, heavy industry, the exploitation of natural resources and the financial sector. It was complementary to the private domestic and multinational, sectors, that is, each ownership sector specialised in specific sectors in the economy where it had the greatest comparative advantage. By the 1970s a large proportion of the steel industry (approximately 70% of capacity) was in the hands of state enterprises. Similarly state enterprises were heavily involved in the exploitation of natural resources, as was the case with Petrobras (Petroleum and various derivative industries) and Vale do Rio Doce (mineral exploitation)[3]. In addition to these areas, public sector ownership was widespread in the field of public utilities, railroad transportation, ports and the banking and financial sector (which includes the gigantic development bank – BNDES, and commercial banks owned either by the federal or state governments).

The importance of the state can also be gauged by the following facts: a) a 1974 survey of the 5113 largest incorporated firms showed that over 39% of assets belonged to SOEs, while these same firms were responsible for 16% of the value of sales; b) a 1985 survey of the 8094 largest firms revealed that the share of net assets of state enterprises amounted to 48%, while the share of these enterprises in total sales totalled 28.1%.[4] The state also had an extremely powerful position in the financial sector.

The loans of the BNDES, together with other federal and state development banks, and official savings banks amounted to about 50% of gross capital formation in 1980s. The state also had a considerable influence in the commercial banking sector. For instance in 1985 the Banco do Brasil (the federally owned commercial bank) held 24% of all funds on deposit in Brazil's 50 largest commercial banks including some commercial banks owned by the state governments. Finally, at the beginning of the 1980s, the national development bank, the national housing bank (now extinct), the Bank of the Northeast and various development banks of individual states, provided more than 70% of the loans devoted to investment purposes. What was the impact of this substantial presence of the state in the Brazilian economy and was it necessarily harmful to the interests of the private sector?

It has been argued that for a long period of time this large-scale presence of the state in the economy was beneficial to both the domestic and foreign-owned private sectors.[5] State firms provided relatively cheap inputs to the private sector (steel, electric power etc.). The state was also the major source of finance for both public and private investment activities. In fact, there was a remarkable growth of savings in the 1960s and 70s which was due to the government sector. The latter created and administered many forced saving funds through various social security levies. For instance, in 1974 64% of Brazil's savings were due to publicly

administered social security funds; by 1980 this had risen to over 70%. All these factors went some way to contributing to the accelerated growth which Brazil enjoyed between 1950 and 1980. However beneficial the impacts regarding growth, the hefty presence of the state failed to address the worsening pattern of income distribution.[6]

The decadence of state enterprises

Already, by the late 1970s a number of weaknesses inherent in the extensive presence of state enterprises had become apparent. The main features of the decadence of state enterprises were the following: a) the use of state enterprises as macroeconomic policy instruments, for instance forcing state enterprises to restrain their prices and tariffs they charged for their products in order to repress inflationary pressures. This did not halt inflation but caused large deficits in the affected enterprises, undermining their efficient operations and forcing the state to subsidise the losses incurred, which in turn, worsened the government deficit; b) the political pressure to over-employ in SOEs and to increasing hire individuals with personal connections to executive positions; c) the increasing number of cases of corruption resulting from the quasimonopoly position of state firms in certain sectors; d) the use of public enterprises to borrow more on the international market than they needed in order to provide the inflow of foreign exchange in order to cope with a deteriorating balance of payments. This placed many SOEs in a precarious financial position.[7]

The privatisation drive of the 1990s

In the 1980s the combination of the debt crisis, the fiscal crisis and bouts of hyperinflation forced Brazil to adopt a set of neo-liberal policies, one of whose main features was privatisation. The pressure to adopt privatisation policies came not only from within, but also from the demands of Brazil's major external creditors, most especially the multilateral organisations, the IMF and the World Bank.[8]

The privatisation experience

Starting timidly in the late 1980s but accelerating markedly after 1994, Brazil engaged in one of the world's largest privatisation programmes. At first privatisation was concentrated in the steel and petrochemicals sectors, later embracing such state firms as the airplane manufacturer Embraer. From 1994 on the privatisation programme expanded rapidly, as it now included public utilities, such as telecommunications, electricity distribution, railroads, ports and some of the major high-

ways. At first foreign participation was limited. After a number of constitutional amendments which allowed foreign firms to participate in public utilities, the involvement of foreign capital in the privatisation process increased dramatically. By 2002, receipts for privatisation amounted to US$ 105.3bn. Of this, foreign participation totalled US$ 42.1bn and on a sectoral basis privatisation of public utilities amounted to 63%.[9]

It is important to note that a substantial source of domestic participation in the privatisation auctions was constituted by the public sector using the resources of forced savings schemes. In this regard, the role of public sector pension schemes should be highlighted. For instance, in the case of the steel industry – among the earliest privatisations – the Banco do Brasil pension fund, Previ, was a key player. By 1997 it had acquired a substantial (23.9%) stake in Acesita (a special steels company) which, in turn, owned important stakes in two other steel enterprises, Indústrias Villares and Aços Villares (De Paula, 1998). Within the same industry, a consortium of other public sector pension funds had managed to acquire a substantial stake in Belgo Mineira, a key enterprise in the speciality steels market. Of course, the role of the public sector pension funds in the privatisation process extended to well beyond the steel sector. In the case of Previ[10], it can be shown that by the end of 2002, the fund had acquired major stakes across a range of key privatised companies.[11]

The role of the state as a regulator

One notable feature of Brazil's privatisation has been the fact that public utility privatisation has been carried out through the granting of concessions rather than a permanent transfer of assets. The winner of the concession contract would be running a facility for a limited period of time (usually 20-25 years) at the end of which the assets would revert to the state unless a new concession would be granted either to the old firm or a newcomer after an appropriate auction. During the concession period, the concession contract would be in force. It would include provisions for rate or tariff readjustments, investment obligations for both maintenance and upgrading the relevant facilities etc. For instance in the telecommunications sector, strict targets have been set for increasing provision of fixed and cellular lines, while service quality is also monitored and enforced.[12]

The administration of the concession contract would be in the hands of special regulatory institutions (e.g. ANATEL; ANEEL) and in some cases government ministries. As one commentator noted the introduction of these agencies established "an array of sectoral regulatory-normative federal agencies that…have changed not only the procedures but indeed the culture of Brazilian public sector management primarily in the area of infrastructure. Previously line ministries or public enterprises

under their jurisdiction have carried out not only policy-making functions but also economic alterations…"[13]

An additional aspect of privatisation through concessions was that the BNDES development bank helped to finance both domestic and foreign bidders in the auction process.

The regulatory state and its economic influence

Since public utilities privatisation through the concessions model had the heaviest weight in the privatisation process, regulation has become one of the most important channels through which the state can influence economic activity.[14] Of the state's various regulatory responsibilities one of the most significant concerns the setting of tariffs. In formulating policy in this regard the state has had to balance the influence of competing constituencies. In the period of rapid privatisation, the state in an effort to attract bidders to its concession auctions prioritised the interests of investors, raising tariffs sharply in order to raise the rate of return and thus attract the maximum number of bidders.[15]

As a result of the regulator's lenient policies towards the new concessionaires, profitability of public utilities increased dramatically. For instance, in the case of electricity generation, from being negative average profitability rose to 1.8% as a percentage of turnover in 1996 to 4.3% in 1999.[16] For the electricity distribution sector, too, the initial years post-privatisation proved a favourable period: between 1995 and 1999 average profitability increased from 4.3% to 5.9%, having been negative for much of the first half of the decade.

An important consequence of privatisation was that the concessionaires were required to substantially upgrade the facilities they administered under the concession contract. This was often made easier by the government through generous loans made to the concessionaires via the BNDES. In the case of the electricity sector, between 1995 and 2000 no less than 43.8% of total investments carried out by the newly privatised utility enterprises was financed using funds from the BNDES. Such funding resulted in a surge in fixed capital formation: between 1994 and 1999 installed capacity in the generating sector leapt from 54.1 GW to 64.0GW.[17] The railroad transportation system has also been realising a quantum leap in investment following its privatisation through the launch of concessions. Once again the BNDES is proving a key player in financing rises in fixed capital formation: between 2000 and 2004 the Bank has committed itself to funding 47% of the projected rise in network capacity.[18]

In the case of the 9945 km of privatised federal and state highways the BNDES has also proven an active participant in the financing of infrastructural improvements. Since the launch of the concessions, the Bank has provided funding amounting to 31% of total investments in highway upgrading.

Political change and its regulatory implications

By 2002 the harmonious relationship between the government and the concessionaires began to unwind. There have been a number of reasons for this. For instance, the high interest rate policies adopted in order to defend the exchange rate contributed to low economic growth and to an increase in the burden of debt incurred by the concessionaires. This was reinforced by the devaluation of the Real in January 1999 and the continued depreciation of the currency throughout up to the final quarter of 2002. The resulting rise in the cost of the debt of many concessionaires made them demand generous increases in their tariffs.

However, as early as 1998 the attitude of the government was already becoming less favourable to the concessionaires and more sympathetic to the needs of the lowincome population and to other hard-pressed users of public utilities. For example, in the case of highway concessions, the protests of associations of truck drivers in various states forced the government to reduce tolls.[19] These reductions, in turn were contested by a number of concessionaires, who went to court claiming that by reducing tolls the government had violated the concession contracts.[20] This demonstrates an early example of the pressures from different groups to which regulators were subject. In the case of the telecommunications sector, the election of the Lula administration appears to herald similar downward pressure on tariffs. At present (2003) telecommunications enterprises are seeking to maintain in place arrangements by which tariffs are adjusted in line with general price inflation. However, according to the Minister for Communications, Miro Teixeira, this regulatory approach is unlikely to survive for long with the "elimination of rate indexation and the promotion of increased competition."[21]

In 2003, downward pressures on tariffs had resulted in a potential change of the ownership landscape as there were signs that some concessionaires were seriously thinking of abandoning their concession contracts, resulting in a process of renationalisation.

Another key regulatory issue faced by the concessionaires in the wake of privatisation has had less to do with the level of tariffs *per se* than with uncertainty over their future path and the transparency which attaches to their setting and enforcement. In this regard, the performance of some of the regulatory agencies has been more investor-friendly than others. In the case of the electrical energy sector, for example, the regulator, ANEEL, has come under consistent criticism for the opacity, complexity and inconsistency of its management of tariff setting. For Landau (2002, p.5) ANEEL comes in for criticism "for its failure to adopt clear, unequivocal and rational rules on tarification. This factor has contributed significantly to insufficient private investment in power generation (because investors did not know the relative prices of inputs and outputs of generation plant, leading to shortages..)."

Achievements and failures of regulation: the contrasting fortunes of electricity and telecommunications

Of course, it should be recognised that the post privatisation period in Brazil has been associated with regulatory achievements as well as failures. The case of telecommunications offers a sharp contrast with that of electrical energy. The telecommunications regulator, ANATEL, has succeeded in presiding over a surge in both capacity and in competition whether in the fields of fixed line or mobile services.[22] However, the experience of the electrical energy sector has proven far less favourable, a conclusion underlined by the power shortages and outages that plagued Brazil in 2001-2. What factors can help account for this apparent contrast in fortunes?

In first place, it is important to recognise the fundamentally different technological drivers affecting Brazilian electrical and telecommunications utilities. Although both classic "network industries", the telecommunications sector has in the past 10 years witnessed a far more rapidly moving technological frontier than electricity. One consequence of this is that the unit cost of furnishing capacity in telecommunications has rapidly fallen as technologies such as fibre-optic transmission and digital exchanges have been diffused. At the same time, the introduction of cellular telecommunications technology (in particular high-capacity digital networks) has greatly enhanced the capability of utilities to provide voice and data services to consumers and, for the first time, to offer a real alternative to fixed line networks. The effects of these fundamental technological facts (which are all too often ignored in the regulatory debate in Brazil) have been, above and beyond the ability to deliver rapidly increased capacity, to challenge the very nature of telecommunications as a classic natural monopoly.

In the case of electricity, by contrast, the pace of technological change has been far more restricted while Brazil has remained overwhelmingly reliant on hydro-electric power. Whatever regulatory regime might have been applied would have had to face this reality and to recognise the relative supply inelasticity inherent in it. Nevertheless, it is undeniable that difficulties of the electricity sector – in particular the arrival of the power supply crisis – could have been avoided had additional (especially thermal and long-distance transmission)[23] capacity been available. The fact that events unfolded differently, and that sector performance was so much poorer than telecommunications, must therefore be viewed in part as a regulatory artefact.

There are a number of reasons that help explain why this was the case. First, as Goldstein & Pires (2001) point out, there is the question of timing. Unlike its counterpart in telecommunications, the electricity regulator, ANEEL, was not established at the outset of privatisation, rather coming into being once the process was underway. According to Goldstein & Pires (2001, p.21) this led to its "legitimacy in dispute settlement and arbitration (being) contested". According to Salgado (2003)

these problems were compounded by the continuing co-existence of public sector enterprises (such as Chesf and Furnas) with private sector ones, a situation quite unlike that in telecommunications. The lingering role of the state as owner as well as its newly established one as regulator not unsurprisingly led to conflicts of interest. The sense that there were privileged players within the generating sector is one of a number of factors which help to explain why private sector investment in it has proven so restricted. More generally, Salgado (2003) notes that an inconsistency of important contractual rules, especially between generators and distributors across the sector, has made ANEEL's task very complex and has certainly retarded efforts to stimulate the entry of new investors.

Aside from uncertainty and complexity regarding the regulatory framework in electricity, it is also worth noting that, in at least partial contrast to telecommunications, the problem is one of regulatory governance and institutional development itself. As Goldstein and Pires (2001, p.21) put it: "as most of ANEEL's top management is formed by former DNAEE[24] officials, the signal given to private investors is that the crux of the regulatory game still concerns technical, legal and operational issues, and not the creation of the economic incentives necessary to create a really competitive market". In addition, it should be pointed out that one key aspect of ANEEL's external institutional relations, that with the oil and water regulators (ANP and ANA), has not been coordinated in an efficient or effective manner. Thus, critical issues for the electricity generating sector such as the development of water and gas resources have not been addressed in an inter-departmentally "joined-up" or integrated fashion.

The government of President Lula da Silva, public utilities and the future evolution of the regulatory state

From the foregoing, the appropriate conclusion would seem for the electricity regulator, to emulate in some sense the experience of the telecommunications sector[25], and to develop investor-friendly regulatory regimes which have as their core a focus on transparency, predictability and, above all, a commitment to setting tariffs designed to stimulate growth in capacity.[26]

While this appears valid within a permanently privatised public utilities setting, it implies that the socio-political preferences of society will not change and that, therefore, it is possible for the regulatory agencies to be permanently inclined towards favouring the private investor. We have, however shown in this article that in a democratic regime there may be substantial swings in the mood and preferences of society. If, for any reason, this mood swings in the direction of more populist policies, that is, placing equity above the need to entice investors, the possibility of more lasting guarantees facing investors will not be possible.

With the election of President Lula da Silva in October 2002 the regulatory agencies established under President Cardoso have come under acute pressure. According to a recent article in the *Washington Times*, President da Silva is seeking to curb the regulators' powers after having accused these agencies of having overseen excessively investor-friendly pricing regimes. In particular, President da Silva was quoted as stating that "(the regulators) are procuring the political power of Brazil. They've created a wall between themselves and the government."The article further states that the new president and his team have been studying the country's regulators, targeting them for changes which are said to benefit certain sectors more than the population in general. Among the issues of contention between the government and the regulators is the linkage of price rises for intermediate inputs such as steel and ethanol to movements in the US Dollar. The article further states that the new government has put the brakes on recent attempts to increase energy rates by more than 40% over the next four years.

Finally, a Senator Aloizio Mercadante, a confidant of the president, and the government's leader in the Senate said that "there are serious problems with the agencies, from the area of tariffs to that of regulation. The government has lost the ability to regulate important sectors such as utilities." Another politician close to the president, Congressman Roberto Jefferson stated that "we are certain that the regulators (are acting) above the law." "They're treated like a parallel power. I think the performance of these agencies is really an abuse."[27]

Changes in the political atmosphere alluded to above could also manifest themselves in the government's policy regarding the appointment of key personnel to the regulatory agencies.[28] Landau (2002, p.8-9) has observed that up to the end of the Cardoso administration the government gave preference in its nominations to "expertise over partisan allegiance or the exchange of political favours, but the vagaries of politics in the future may intrude on this very sensitive process. The outstanding example of an agency governed by personalities of acknowledged stature is ANATEL, whose resolutions tends to be politically neutral whereas ANEEL, where nominations are made on the basis of political rather than technical criteria, has often produced resolutions that result in controversy, to say the least, and that are disputed (often in court) by both concession-holders and consumer groups."

Another perceptive observation relating to the inevitably political nature of the regulatory mission emerges from a recent international report.[29] The report draws attention to the fact that "it is one thing for countries to make a policy decision to create an independent regulatory agency, and quite another to empower the agency to act independently and effectively… Inevitably (regulatory agencies) are the products of political, social and legal conditions that exist at fixed points in time, in each country… regulatory approaches and policies change, and agencies change with them" (International Telecommunications Union, 2001 p.1).

Some might even doubt that investor-friendly regulatory policies will attract a substantial amount of private investment. As we have indicated, a large proportion of the financing of public utilities in Brazil was supplied by the BNDES using public money. Were the financially parlous state of the utilities sector to result in its progressive re-nationalisation then, in the absence of investor friendly regulatory policies, much needed increases in investment could only be implemented through either direct subsidies of consumers or through direct public sector capital investment. In other words, it is ironic that whether the administration of public utilities remains within the private sector or reverts to direct government control, then in either case the resources of the state will always be required to sustain investment programmes. Of course, one might take the view that, whatever the role of the state in providing capital, these resources might be used more efficiently used by privately administered entities.

At the beginning of the 21st Century it would seem that the major influence of the state on economic activities is through its regulatory agencies and through the development bank. Through regulation it influences the country's electric power supply, its telecommunications system, its rail and road transportation network, its oil exploration and production sector (both through the still publicly owned Petrobras and the regulation of the activities of foreign oil prospectors). In addition, the state development bank is still the major source of investment funds. Through these instruments – both as a regulator and as financier – the state continues to exercise a major influence over the development of these sectors. More specifically, given the existence of thin capital markets – which necessitate borrowing at subsidised interest rates – and regulated prices, two of the most important dimensions of the economic environment faced by "privatised" enterprises are set by the state.

Above and beyond any regulatory or financing role, it should be remembered that the state has not entirely relinquished its position as the channel through which savings are accumulated (forced savings through pension funds) and then directed at favoured sectors. We have shown among the most favoured sectors have been the privatised utilities and such industries as steel.

With a depressed domestic market, and the financially parlous state of many multinational utilities groups (especially in telecommunications) many enterprises in the Brazilian utilities sector have been experiencing liquidity problems which the state is increasingly less willing to address through favourable tariff adjustments. This may lead many of the concessionaires to abandon their contracts, in essence leading to a "re nationalisation" of the utility.

An interesting example of the difficult current (2003) state of the utilities sector is provided by the case of Eletropaulo, the São Paulo electricity distributor whose concession was obtained by the US group AES in 1998. AES has run into difficulties with its Brazilian subsidiary as tariffs and consequently revenues have failed to rise in line

with the enterprise's debt payment obligations to its creditors, most especially the BNDES. Owing the BNDES US$ 1.13bn of which US$ 600 million is past due, AES has found itself – temporarily at least – unable to continue with its repayments, triggering heated negotiations between itself and the Bank. The regulatory and financial conflict between AES and organs of the Brazilian state has now become something of a test case regarding public policy response to the deteriorating condition of the utilities sector. Mindful of the implications for other foreign investors, the US State Department has become involved with the US Ambassador to Brazil attempting to intercede.[30]

AES/Eletropaulo is not the only example of a foreign-owned utility in financial difficulties. In the case of the French-owned EDF, its Rio de Janeiro electricity distributor, LIGHT, owes more than US$ 125 million to a consortium of domestic and foreign banks.[31] In addition, the Minas Gerais – based distributor SEB/CEMIG (also partially-owned by AES) is overdue on some US$ 87 million debt payment to the BNDES.

While in many regards, the liberalisation of the Brazilian telecommunications sector has proved more successful than in the case of electricity, the sector may nevertheless face serious problems. In particular, some enterprises will struggle to extract themselves from the trap of heavy indebtedness and lack of liquidity. These problems initially surfaced following the depreciation of the Real in early 1999. Since then, a number of service providers have been struggling to meet their debt obligations, faced with a mismatch between foreign currency denominated debts and local currency denominated revenue streams. To make matters worse, revenues have been constrained by a combination of price regulation and the failure of market demand to expand to the extent originally anticipated. In the most recent casualty of these unfavourable conditions, the São Paulo cellular service operator BCP was taken over by its creditors in April 2003, forcing the exit of a major US shareholder, Bell South.

In order to prevent future recurrences of such cases, the authorities would need to ensure that tariff alterations appropriately reflected the evolving cost base of telecommunications enterprises. On this score, the outlook for the sector is not especially favourable. In June 2003, hot on the heels of criticism from President da Silva himself, a series of legal injunctions overturned Anatel-agreed tariff increases nationwide.[32] More troublingly still for Anatel, a draft presidential decree released in May 2003 mandated the handing back of much responsibility for the oversight of the telecommunications sector from the regulatory agency to the Ministry for Communications. In particular, the decree requires that Anatel be stripped of its decision-making functions in terms of tariff setting and the establishment of service obligation rules. So long as uncertainty continues to surround the regulation of the telecommunications sector, it is difficult to envisage a renewed wave of investment of the type experienced in the 1990s.

Perhaps the firmest statement to date of the Lula government's intent regarding the regulation of public utilities came at the end of 2003 with the announcement of

a Presidential decree establishing a New Model for the electricity sector (IPEA, 2003). The measures contained in the decree reflect two key policy precepts that have emerged in the government's other pronouncements on public utilities; that regulation should be increasingly "repatriated" to the ministries from the agencies and that the thrust of policy should aim at delivering low tariffs over the longer term in order to realise social objectives.

Pursuant to these guiding principles, the New Model mandates that future tenders for generation projects be evaluated not on the basis of the most modest use of public funds but on their ability to deliver the lowest tariffs (ibid. p.26). In addition, decisions over the award of such tenders will be made by the Ministry of Mines and Energy (MME) and not, as hitherto, by ANEEL. This represents a real stripping away of power from the regulator and could presage yet further centralisation of regulatory functions by the MME. The other key provision of the Model strengthens the sanctions against distributors who experience difficulties in making payments to their suppliers. Since the state remains a key player in the generation market while the private sector predominates to a much greater extent in the distribution sector, this represents a clear manipulation of regulatory policy in the direct interest of the public sector.

The current direction of policy and the not unrelated sickly state of many privatelyowned utility providers clearly raises an important issue for the government: can it any longer attract the bidding of new concessionaires, and in order to do this, would it be obliged to offer more generous tariff conditions? If the re-nationalised enterprises should remain in the hands of the public sector, would the state be in a position to run a deficit-generating public utility? If the latter, the implication may be that there would be a decline in the rate of return accruing to the investments of the "forced savers" administered by the BNDES. In the past such a reduction in the rate of return may have been feasible against the backdrop of a relatively young population. Nowadays, however, with an ageing population relying increasingly on savings through the social security system, there would be less scope for such financing arrangements.

Even in the non-public utility sectors which were privatised in the 1990s but whose new owners were also heavily indebted to the development bank, what would happen if due to difficult economic conditions, that is, lower growth and higher interest rates, the owners of these firms defaulted? In this eventuality it appears probable that their debt to the BNDES would have to be converted into ownership shares. Thus, a form of re-nationalisation would occur.

Conclusion

In this article we have shown that Brazil's economy in the aftermath of privatisation has not become as fully exposed to market forces as one might have expected. All of the important public utilities sectors are subject to substantial regulation and a large

proportion of all productive sectors remain dependent on the state for investment financing. We would not wish to pretend that the post privatisation period has witnessed no meaningful alteration in the scope of state intervention in the productive sector. In particular it should be emphasised that privatised enterprises now have much greater control over their internal functioning, their cost base and, most important of all the size and composition of their labour force which is no longer subject to political interference.[33]

However, we have shown that a more populist stance in regulating public utilities and the precariousness of the debtors of the development bank (due to interest and exchange rate movements) may augur a period of progressive re-nationalisation and, at the same time, could jeopardise the security of the forced savings of the public. It is thus more than clear that the functioning of the Brazilian economy will not be subject solely to market forces but will continue to be strongly influenced by the actions of the state.

NOTES

1 School of Economic Studies, University of Manchester

2 University of Illinois at Urbana-Champaign

3 For details see Baer (2001) Ch. 12 and Amann, De Paula and Ferraz (2002) and also Baer (1969)

4 Baer (2001)

5 See Evans (1979), Amann (2000), Baer (2001)

6 Wells (1976) Werneck (1986)

7 Baer (2001, pp. 283-284)

8 Castelar Pinheiro (1999)

9 BNDES *Privatização no Brasil* (2003)

10 Previ had by the end of the 1990s acquired a 13.8% stake in CSN, Brazil's largest and oldes steel company (Amann, De Paula & Ferraz, 2002)

11 For instance, among Previ's R$13.4bn in total equity holdings in December 2002 the following privatised companies featured prominently: Acesita R$39M; Brasil Telecom R$143M; Eletropaulo R$22M; Embraer R$852M; CVRD R$307M (Source: Previ Annual Report 2002)

12 BNDES (2000, p.9)

13 Landau, Georges 'The regulatory-normative framework in Brazil', *Policy Papers on the Americas,* Vol. XIII, Study 2 April 2002 p.2 CSIS, Washington D.C.

14 For a comprehensive review of the rise of the regulatory state in alternative national contexts see Glaeser and Shleifer (2003)

15 In the city of Rio de Janeiro, for example, while the consumer price index rose by 189.7% between August 1994 and February 2000, the price index for public services rose by 264.7%.

16 BNDES (2000b)

17 ibid.

18 BNDES (2000c)

19 In 1998 truck driver protests resulted in a 50% reduction in tolls; in 1999 tolls were reduced between 20 and 28% and in July 1999 there was a brief national truckers' strike demanding a toll reduction.

20 BNDES Seminário de Privatização, November 2000

21 *Brazil Focus* David Fleischer, 24th February 2003

22 International Telecommunications Union (2001) Another comprehensive review of the accomplishments in the telecommunications area can be found in a chapter by Siqueira in Lamounier & Figueiredo (eds.) 2002 pp. 215-240. The same volume also contains a chapter on the accomplishments in the transport sector written by De Toledo pp. 241-292

23 Much long distance high-voltage transmission capacity remains in the hands of the state. Efforts to boost private investment in this sector have been particularly hampered by regulatory uncertainty and constant changes in stance by ANEEL (Goldstein & Pires, 2001)

24 The government department responsible for sector regulation prior to privatisation.

25 We do not of course wish to pretend that the telecommunications sector has been without its problems: as will be seen recent anaemic growth in revenues allied to foreign currency linked debt have taken their toll and are prompting a process of corporate restructuring.

26 José Claudio Linhares Pires, Fabio Giambiagi and André Franco Sales, 'As perspectives do setor eletrico após o racionamento', *Revista do BNDES*, 18, Dezembro de 2002 pp. 163-203

27 (Article by Bradley Brooks 'Brazil may curb regulators' powers', *The Washington Times* February 20th 2003)

28 This is also emphasised in a general survey of Latin America's electricity sector: see Fischer & Serra (2000, pp.188-189), Spiller & Cardilli (1997) and Spiller & Viana-Martorell (1996)

29 International Telecommunications Union, *Effective Regulation Case Study: Brazil,* 2001

30 *Estado de São Paulo,* 12th and 13th March 2003; *Jornal do Brasil,* 12th March 2003

31 VALOR, 2 Julho de 2003, p. B 1.

32 A 41.7% readjustment of rates which had been authorised by Anatel was suspended by the Court of Justice of Rio de Janeiro *Jornal do Brasil,* June 30th 2003 p. A7.

33 In the case of the railroad sector, for example, employment since privatisation has declined substantially. Employment in that part of the railroad network formerly controlled by the RFFSA has fallen from 28,639 in 1996 to 12,807 in 2000 (Ministério de Transportes, 2000).

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Edmund Amann

Professor of Economics,
School of Economics, University of Manchester, UK

Werner Baer

University of Illinois at Urbana-Champaign

REGULATION AND DEVELOPMENT: REFLECTIONS IN THE AFTERMATH OF NEOLIBERALISM

Luciano G. Coutinho

INTRODUCTION

The neoliberal offensive of the 1990s aimed to extend the paradigm of competition into every sphere as a means of achieving social welfare and efficiency. In doctrinal terms promoting the combination privatization-plus-competition became an end in itself. By ignoring the strength of scale and scope economies, and by imagining it was possible to dismantle or dismember the large, capital-intensive network infrastructure systems characteristic of major public utilities with no counterproductive after-effects, this utopia caused failures and waste. Attempts to break up these activities horizontally and/or vertically, especially in the United Kingdom and United States, were mostly ineffectual. They destroyed the economies of scale and integration without achieving lasting gains in terms of efficiency, quality and lower user charges. Several examples can be found in the power and transportation sectors.

The first lesson is that privatization and competition worked well in typically private segments such as industries that had been developed or absorbed by the state owing to the fragility of their capital structure when in private hands (e.g. steel, mining, shipbuilding or petrochemicals). In infrastructure and public services (telecommunications, energy, water supply, transportation etc) the experience was problematical, however. Except in telecom, where a technological revolution has modified the conditions that gave rise to the original natural monopoly while creating new opportunities for profitable business models in the private sector (e.g. wireless and mobile telephony, Internet service etc), the neoliberal paradigm has produced mediocre results. In natural monopolies, where scale economies are powerful,

investments take a long time to mature and externalities are present, the private model tends to run into difficulties hard to overcome.

The social mission intrinsic to infrastructures that provide public services and utilities is indeed basically incompatible with the private investor's goal of maximizing profit. This investor requires far higher rates of return on his capital, and relative prices therefore logically need to be higher in order to remunerate capital at such high rates. This paper argues that the choice of a basic model — public or private — should be preceded by a comprehensive and painstaking review of the pros and cons of each option. Under certain conditions, privatization combined with light and efficient regulation can reconcile the objectives of generating private returns and maximizing social utility. Under other conditions, the option for maintaining a public monopoly operated by state-owned enterprises with efficient management may offer a better alternative, facilitating a convergence between returns to capital and to society.

The regulatory framework and planning conditions — indispensable in either case, it is argued here — should obviously correspond to and be compatible with the characteristics of the operating model chosen.

1 The baselessness of the competitive optimizing paradigm

The foundations of the neoliberal paradigm rest on a belief in the efficiency, if not the perfection, of markets as inducers of solutions that maximize welfare (Pareto optimality). According to this postulate (which ignores or belittles the presence of scale economies and externalities, disregards transactions costs, and moreover underestimates the importance of republican practice in democratic regimes), public regulation is assumed always to be inherently spurious, suboptimal and conducive to corruption.[1] The normative prescription of this paradigm is as radical as its foundations are unrealistic: regulation is to be scrapped, everything is to be privatized, and the role of the state is to be minimized, leaving only its role as guarantor of private property rights; competition should be created forcibly whenever it is "impeded", even if this requires the dismemberment of the large corporations and respective monopolistic or oligopolistic structures.

The paradigm rests on unrealistic foundations first of all because it assumes diseconomies of scale and the existence of a large number of producers. This is simply not the case in the real world. Or when it is the case, it is an exception. Small producers predominate in few sectors of modern economies (mainly services). In fact, the dominant industrial paradigm is the oligopoly, with a small number of large players competing on the basis of constant returns to scale in the market space most relevant for price formation. In many sectors, however, scale economies are more powerful — increasing returns are obtained (falling unit costs) and this leads to higher levels of oligopolistic concentration and, at the extreme, to monopoly.[2]

In proposing and potentially implementing the fragmentation of efficient monopolies (or oligopolies) with the aim of generating competition, neoliberal policy makers ignore increasing returns to scale and risk introducing inefficient solutions. However, when challenged about this risk the most sophisticated theoreticians recommend more moderate therapies to introduce competitive mechanisms. One prescription is forced sharing of the monopolist's infrastructure by new entrants (e.g. competitive "mirror" startups v. incumbents in the case of telephony). As shown below, however, mechanisms designed to introduce or mimic competition are often counterproductive as far as promoting social welfare is concerned and may constitute inferior solutions in terms of productive, allocative and distributive efficiency.

In short, increasing returns to scale are an important and irrefutable part of the real world. Moreover, they determine that the maximization of economic efficiency generally requires large fixed-capital structures and a substantial concentration of market power. This makes the need for regulation unavoidable. Public regulation (sector and/or anti-trust) that directly oversees the conduct and performance of these structures can generate more efficient solutions from the economic and social standpoints under certain conditions, as will be shown below. Rejection of regulation coupled with unconditional adoption of the private model and forcible introduction of competition may well be incompatible with the goal of maximizing social utility, not to mention the need for major investment in infrastructure in developing economies.

2 Intense competition in oligopolistic structures

Oligopoly — the market structure most often found in industrialized economies — does not necessarily entail an absence of competition. On the contrary, in fact, in conditions of rapid technological innovation oligopolistic competition tends to be more intense and aggressive (compared with the idealized paradigm of perfect competition). Oligopolistic competition usually takes place in a climate of strong rivalry, using strategies of pre-emption or mutual deterrence that result in cycles of simultaneous investment by the rivals. These cycles often generate high levels of excess capacity — levels that are "unplanned" in the sense that they go far beyond the margins of idle capacity desired by the companies participating in the oligopoly. In these conditions of vast excess capacity, if companies face weak markets there is more opportunity for sporadic price wars.

Competitive oligopolistic structures can occur in markets with various configurations (differentiated or undifferentiated goods and services, durables or non-durables), since the key variable is whether the conditions exist to challenge the dominant players, i.e. market contestability and entry/exit barriers. If such conditions exist, antitrust regulation can assume a stance of relative laxity. The risks in this case

have to do not with large players' abuse of their dominant position but with frequent collapse or bankruptcy (due to overinvestment), and all the negative consequences these events may mean for consumers or users. In such cases the regulators should be concerned above all with avoiding the excesses of out-and-out competition.

3 Cartelizing oligopolies and cartels

In conditions of low market contestability (high entry/exit barriers) and/or slowness with controllability and/or imitability of technological progress by the firms participating in the oligopoly, competition tends to be replaced by cartelizing behavior. This behavior comprises practices that include market segmentation and/or regionalization, price fixing and, at the extreme, coordination of decisions to invest and introduce innovations.

This latter point, however, depends on a calculation about the degree to which technological progress could be monopolized. Easily imitable innovations do not undermine cartelizing practices, whereas product or process innovations that can be protected with patents and are hard to reproduce by reverse engineering may tempt the firm that owns them to use them as a weapon to outdistance others through offensive market gain strategies at odds with cartelizing practices.

For these reasons antitrust regulation is essential in such cases but should not be confined simply to inefficient attempts to break up oligopolies to the detriment of scale economies. The focus of regulation should properly be on conditions for market entry and diffusion of innovations (e.g. facilitating entry by removing barriers and protection), complemented by an explicit and vigorous policy of enforcement of antitrust laws and punishment of cartelizing behavior.

4 Natural monopolies, network infrastructures and externalities

Significant increasing returns to scale can create unbeatable cost advantages and lead to market domination by a single entrepreneur. The usual origin of increasing returns to scale is dilution of high fixed cost as revenue expands without a marginal increase in variable cost (which tends to be constant relative to operating scale). In general, large infrastructures in the form of highly capital-intensive networks (e.g. water supply, sanitation, power distribution, transportation, landline telephony etc) are subject to increasing returns to scale due to dilution of fixed cost, constituting natural monopolies. The fact that public utilities are natural monopolies is no coincidence, since by nature these services are intrinsically designed to serve as many people as possible and thus entail a need to develop large-scale networks.

Given the essential nature of public services, the relative amplitude of their infrastructure networks makes them bearers of positive externalities for social welfare,

by virtue of integration effects or other related effects that also increase social benefits. To maximize the social utility of these services they must pursue universalization, thus extending beyond the limits of the market, i.e. the limits dictated by minimally profitable exploitation taking into account the affordability of prices within the scope of most people's income.

This cluster of characteristics — monopolies based on strong returns to scale, high capital intensity and long payback periods, network structures tending to produce positive externalities, and a social mission — not only makes public regulation absolutely necessary but also, as we shall see, requires that these characteristics be specifically comprehended before planning privatization or the introduction of competition. Ideological generalization of the neoliberal paradigm (privatization-deregulation) without taking sectoral specificities into account tends merely to cause economic efficiency, contradicts the social mission of public utilities, and is inadequate to deal with the effects of externalities.

5 Imperfect conditions for matching the private model to public utility sectors

The basic tension between the private business model whose aim is to maximize rates of return in conditions of capital scarcity and the provision of essential public services resides in the nature of the latters' social mission. As already noted, this mission entails the obligation to seek maximum social coverage (ideally universalization) whereas private maximization of rates of return is governed by criteria for calculating the profitability of service offerings so as to obtain the largest possible volume of profit in given cost and demand conditions.

Private investors usually expect very high rates of return (which reflect the scarcity of capital and the specific risks of private ventures and, in the case of Latin America, reflected and still reflect very high spreads for sovereign risk) in comparison with the rate of return that is socially desirable or practiced in the public sphere.[3] The highly capital-intensive nature of infrastructure sectors, which require investors to risk large volumes of their own equity capital, tends to make this contradiction even more acute. By demanding higher rates of return, private investors oblige utilities to set higher prices so that their assets and other capital holdings are adequately remunerated, and these high charges mean the low-income segment of the population cannot afford the services.

For this reason, to attenuate the risk of social exclusion the government (directly or via a regulatory agency) must establish cross-subsidy schemes or introduce subsidies into its budget in order to extend social coverage (ideally targeting universal access). Contrary to the neoliberal prescription, competition is ineffectual in such cases. If it were possible to introduce competition (via forced infrastructure sharing

by new entrants), this would naturally tend to generate an intense dispute for the most profitable market segments (business customers and high-income users). Prices would fall in those segments, while the service offering for low-income users would contract or be downgraded. In other words, competition would probably erode the source of funding for cross-subsidies (high profit rates in high-income markets). Thus the imposition of calibrated universal-access targets upon monopolist licensees, forcing them to transfer extraordinary profits in the form of benefits to low-income users, seems to be a solution that approaches the maximization of social utility.

However, calibrating and benchmarking such targets is no simple task. If regulation is too heavy it may inhibit investment in expansion of the system. Because the large amounts of fixed capital invested in infrastructure are "sunk costs" (non-recoverable fixed costs), the regulator can be tempted to maximize targets or social benefits in the knowledge that the licensee has an interest in offering such services provided it can at least cover the variable cost. But in this situation prices would not cover amortization of fixed capital at the desired rate of return. As a result, without being able to obtain the desired return on investment and without guarantees that protect them from redistributive conduct by the regulator ("regulatory risk" in the jargon of the private calculus), investors would abstain from injecting more capital.

These considerations illustrate the argument that the presence of substantial market imperfections requires intervention by public regulators, while underlining on the other hand the need to ensure that this intervention is not so burdensome for private licensees that it reduces their propensity to invest in network expansion or even brings investment to a halt. In some cases it may be very difficult or impossible for the regulator to reconcile the maximization of social benefits with the private investor's requirement of satisfactory profitability. Under such conditions the concession or license could be granted to a public-sector enterprise, which in theory would be better suited to offer the services because it could operate at a far lower rate of return.

6 Deficiencies of the statist solution

If opting to delegate public service provision to a state-owned enterprise tends to be a superior solution in welfare terms because a utility in the public sector can operate at a lower rate of return better suited to the social nature of the service, and because it has more affinity with long-term planning, on the other hand this solution involves important risks of inefficiency. State-owned enterprises tend to be more vulnerable to politicization and corporatism, especially in the absence of a system of governance with transparency and rules designed to foster productivity and efficiency.

Bureaucratic rules, tax laws, accountability, and public controls (audits etc) tend to establish a framework that restricts freedom of management for state-owned

enterprises. This in and of itself may result in higher costs, slow decision making, and sluggish execution. At the same time these legal and regulatory constraints tend to fuel practices of self-protection and risk aversion, which may distort management decisions.

State-owned enterprises also face risks of instrumentalization by government in pursuit of its own priorities (they may be used as vehicles for external or internal indebtedness, for example, or to carry out other policies, relating to regional, industrial or technological development etc). In governmental and political systems with little transparency, state-owned enterprises can be instrumentalized by the powers that be and become vulnerable to clientelism, cronyism, corruption, and inefficiency in adjusting costs if this causes losses (e.g. jobs, contracts, procurement) for their respective clienteles. The fact that they operate monopolistic infrastructures creates the risk of transferring these inefficiencies to society, either through higher prices (in stark contrast with the reason for preferring state ownership in the first place) or via recognition of losses that will have to be assumed by the government. The worst possible outcome for society is one in which inflated operating costs are combined with underinvestment.

7 Possibilities for rehabilitating state ownership

Recognition of the risks and deficiencies of state ownership, however, should not lead ineluctably to the conclusion that private ownership is the only possible option, especially if it is extremely cumbersome or costly to ensure that private enterprise is compatible with the social obligations of public service provision. On the contrary, the appropriate solution in this case is rehabilitation of state-owned utilities within a regulatory framework that separates the functions of government (political priorities) from those of the regulator (whose mission to protect the public interest should be made explicit for each case) and those of each state-owned enterprise charged with providing public service.

The existence of an independent regulator that focuses on the pursuit of maximum efficiency combined with simultaneous maximization of social benefits should serve to counterbalance the powers of a state-owned monopolist, especially if there are clear rules governing the conduct of its employees, public participation (through hearings and other procedures), and transparency and accountability.

This separation of functions between public regulator and state-owned operator (equally public) should enable the latter to be flexible and take decisions quickly under the non-bureaucratic oversight of the former (based on rules and performance metrics or management contracts rather than discretionary controls). In a democratic regime with a minimum of stability, it is perfectly possible to construct institutional mechanisms of control that discourage the inefficiency and

opacity once characteristic of the state sector (especially in developing economies). Such mechanisms include rewards for efficiency and clear rules governing accountability.

8 Regulation is indispensable and must be specific

Far from being redundant and replaceable with market mechanisms, regulation is indispensable as a means of minimizing the impact of market failures. Furthermore, it is the only way of correcting for the inadequacies of both the private business model applied to public services and the deficiencies of public-sector ownership.

In the case of the private model, the inadequacy derives mainly from the intrinsic requirement of high rates of return, which naturally entails higher prices or user charges than would be sufficient to provide the lower returns suitable to social criteria. There is the additional difficulty of spontaneously ensuring that services are accessible to low-income users, who usually do not provide profitability at the desired level (let alone above it). The public regulator plays a fundamental role in stimulating or conditioning the private operator's performance so as to obtain the widest possible coverage in conditions of reasonable profitability. Cross-subsidies may represent a more efficient mechanism in this regard, although they should be used with prudence in order not to entail excessively high prices for middle- and upper-income users or seriously jeopardize the competitiveness of business users. Moreover, even if cross-subsidies are taken to an extreme they may not be sufficient to ensure that services are affordable to the poorest members of society. In this case extension of services to low-income citizens (especially in countries with highly unequal societies like Brazil) will depend on subsidies allocated directly to the government's budget, although implementation of subsidies in this way is subject to severe constraints for fiscal reasons.

Public regulation is also indispensable to rehabilitate the state ownership model. From the standpoint of rates of return (social and thus lower) and the willingness to run risks in obedience to a long-term government planning scheme, state-owned enterprises are better suited to operate utilities and provide essential public services. However, they are more susceptible to political instrumentalization and "capture" by workforce corporatism and/or vested interests of other kinds (suppliers or management, for example). An independent and impartial public regulator can be charged with introducing rewards for efficiency and measures to deter the distortions typical of state-owned enterprises. In democratic regimes it is perfectly possible to minimize the risk of regulatory capture by vested interests, subjecting regulatory agencies to parliamentary oversight and making them accountable to society as whole within an overall framework designed to ensure transparency and impartiality.

It bears repeating that the choice of model and the design of a regulatory framework require careful case-by-case analysis of all characteristics of each service and the respective network or infrastructure. The choice of model and the corresponding regulatory format therefore depend on objective economic and financial conditions, i.e. capital intensity, sunk costs, payback, working life, amortization, demand characteristics and conditions (degree of essentiality, price and income elasticity), capital cost, borrowing cost, and the speed and other characteristics of technical progress.

Evidently the private model is more easily adjusted to services or networks that are less capital-intensive and have shorter payback periods, besides showing more propensity to technological progress and less demanding requirements as far as universal access is concerned. Conversely, the state ownership model seems in principle to be more adequate for infrastructure with relatively greater capital intensity and longer payback, as well as more significant effects of externalities (not capturable by private operators but relevant to social welfare) and more stringent demands regarding universal access.

9 The challenge of regulating for development: the need for planning

The regulatory framework should evidently be designed in accordance with the characteristics of the model chosen, private or public. Regulation also needs to be specific and compatible with the essentiality of services, with demand conditions (relevant income and price elasticities), with the pattern of technological progress in each sector, and with the efficacy of the possible mechanisms to promote or mimic competition (which under no circumstances should destroy synergies and scale economies in order to avoid introducing counterproductive inefficiencies).

Thus it is no small task to choose the more efficient model and design the most adequate regulatory framework. There is also the complementary, and equally challenging, task of institution building and implementing safeguards to ensure that efficiency, transparency and accountability are built into the regulatory system.

Alongside the challenges of public choice and institution building it is also necessary to assure the expansion of utility infrastructures, especially in developing countries, where such expansion is of paramount importance. For this reason the choice and design of a model that is both as economically efficient as possible and compatible with the social mission of the public services involved must not minimize the importance of assuring their expansion. In developing countries, models for operating/regulating these services should have a pro-investment bias, given the enormous deficit in basic services and the significant external economies generated by infrastructures.

In light of this last point, and considering the potential uncertainty due to the indivisibility of investment in these sectors and the long payback periods involved,

it is most important to give public-sector planning a central role once again. The function of planning in providing signals or guidelines for long-term investment decisions and reducing uncertainty is indispensable and complementary, whichever operating model is adopted, private or public. It is also worth noting that planning will be all the more effective if it is closely linked with the institutions that provide development finance (e.g. domestic public banks and multilateral lenders for long-term credit), whose participation is crucial to reduce capital cost and enable viable funding structures to be engineered for investment in infrastructure. The planning function may or may not be directly subordinated to the regulator. This will depend on the model. In any event it is indispensable that a public, long-term, technically qualified perspective be adopted. The advantage of keeping planning and regulation independent of each other is that institutional separation minimizes potential conflicts of perspective between one agent that focuses on performance oversight and the other whose main concern is driving expansion of the system.

10 Some concluding thoughts

The purpose of this short paper is to demonstrate that the thorny task of the public regulator, who must try to reconcile maximization of social benefits with the need to guarantee satisfactory profitability for the licensee, be it private or state-owned, cannot be accomplished by means of generalizing norms. There is no such thing as an optimal paradigm that can be adopted a priori and dispenses with long-term planning based on an analysis of the specific requirements of each sector. It is impossible to design an efficient model and regulatory framework without understanding the characteristics of the market, the conditions for profitability, the conditions for competition, and the pace of innovations that redefine business models. A holistic understanding of all these factors, based on a long-term view and pro-investment bias, is indispensable to any effort to define the most efficient and appropriate model for each case.

The problem with the weak results observed in Brazil and Latin America is that ideological adherence to the neoliberal paradigm prevented prior reflection of sufficient depth about ways and means of ensuring the proper specification and formatting of the private model and the efficacy of the conditions for competition to be introduced. Nor was anything done institutionally to develop sufficient and proficient regulatory conditions. It now remains to face the even more daunting challenge of correcting what exists and creating efficient and socially benign models for operation and regulation of public service infrastructures, so as to assure their expansion at a fast enough pace to provide adequate support for economic and social development.

NOTES

1 The state is depicted as a "bête noire" packed with bureaucrats eager to create difficulties in order to sell facilities, serving interest groups that allegedly buttress the bureaucracy to fabricate privilege and protections in order to extract rent from them. Thus regulators are suspected of having their own agenda (maximization of power and prestige) and, the argument concludes, are highly prone to deviant behavior and corruption.

2 Economies of scale exist not just at the level of manufacturing plants but also in the sphere of the business structures that comprise activities such as management, finance and marketing. The existence of relatively high transaction costs represents another factor that determines the capture of scale economies by taking certain activities into the structure of large corporations. Thus to understand the causes of increasing returns to scale at the level of the business organization it is not enough to observe technical economies of scale circumscribed to production (at the level of the plant).

3 The private rate of return utilized as the basis for investment decisions is usually a weighted average of the desired rate of return on equity and the "cost" of borrowed capital (in the form of bank loans and/or bonds issued in the capital market). The desired return on equity is usually higher than the cost of borrowed money. In most cases of privatization in Latin America in the 1990s the required return on equity was in the range of 18%-20% per annum, a very high rate. This is why services had to be priced relatively high.

Prof. Luciano G. Coutinho

Professor of Economics at
University of Campinas - UNICAMP

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REVISTA DIREITO GV *(FGV-SP Law Review) is a journal that publishes articles, book reviews and essays on several fields of Brazilian, international and global law. It also publishes research works and papers on theory of law, sociology of law, philosophy of law and history of law.*

This journal is opened to different theoretical and methodological approaches, including interdisciplinary papers and articles that fall into law & society and law & economics research fields. It also reviews and publishes papers concerned with techniques for teaching law and law research methods.

The 'book reviews and essays' section aims to attract readers' attention to local and foreign books and magazines thus raising critical discussions. Books of academic interest are preferred to those primarily focused on professional use. Essays are format-free, and selected by relevance and novelty. The journal only publishes articles and papers not previously published elsewhere.

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Every article is reviewed by the Editor, who assesses whether or not it fits the journal editorial policy. The article is then sent to two anonymous referees who evaluate qualitatively its content and style in accordance with blind peer review principles. Referees take 45 to 60 days to provide their comments, that will be forwarded to the author for acknowledgment or improvement. In this latter case, a modified text can be sent to the journal to be re-evaluated. Authors will be emailed about the status of evaluation process, being able to access referees' comments on their article. Exceptionally there can be invitations for articles made by the Editor.

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Articles, essays and book reviews must be written in Portuguese, Spanish or English, and must not have been published elsewhere.

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Articles *must have a maximum of 30 pages of 2100 characters. They must also be written according to ABNT (Brazilian Technical Norms Association) standards. Longer papers can be published subject to editor's evaluation.*

Book reviews *must have a maximum of 10 pages of 2100 characters, preferably without footnotes. They must have a title and do not need to be preceded by an abstract. Suggestions for foreign books and magazines to be reviewed can be sent to the editor by email.* ***Essays*** *must have a maximum of 15 pages of 2100 characters.*

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LINHA EDITORIAL

A **REVISTA DIREITO GV** é generalista. Publica artigos, resenhas e ensaios inéditos sobre a dogmática das diversas áreas do Direito nacional, internacional e global, além de trabalhos de pesquisa aplicada e textos de Teoria do Direito, Sociologia do Direito, Filosofia do Direito e História do Direito.

A revista está aberta às mais diversas abordagens teóricas e metodológicas, inclusive a textos interdisciplinares e artigos que se enquadrem no campo de pesquisa *Law & Society* e *Law & Economics*. Ademais, contém trabalhos sobre ensino e pesquisa em Direito.

A seção de resenhas e ensaios tem como objetivo chamar a atenção dos leitores para livros e revistas, nacionais e estrangeiros, e suscitar discussões críticas sobre eles. Além disso visa a divulgar ensaios relevantes para a compreensão do Direito. As resenhas dão privilégio a títulos de interesse acadêmico em detrimento de publicações de uso profissional. Os ensaios possuem forma livre e são selecionados por sua relevância e novidade.

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ISSN 1808 - 2432