

STAKEHOLDERS AND THE MACHINE : IDENTITY AND THE CONSTRUCTION OF RULES ON MONEY

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Policy-makers who develop standards and rules for the financial markets, whether they work in transnational or domestic fora, use consultation exercises to take account of the views of people and firms they characterize as stakeholders. The paper argues that the construction of the concept of the stakeholder in consultations is critical. In some contexts identifying specific stakeholders who may be affected by proposed regulations may encourage people who might not otherwise focus on the consultation to consider responding. But not identifying people as stakeholders, even if they might be affected by the proposed rules, might tend to prevent those excluded from focusing on the proposals and from responding. The global financial crisis has shown that we may all be affected by rules of financial regulation (even at the other side of the world). But although the stakeholder concept is intended to be inclusive it necessarily excludes some members of the world's population. Accountability to stakeholders is necessarily a limited form of accountability.

Requests for comment and consultation documents frequently identify specific categories of stakeholder who may be affected by or interested in the questions raised by the consultation. Response forms and/or consultation documents may invite or require respondents to categorize themselves. But consultation documents and questionnaires do not explicitly address the issue of how they define, or why they do not define, the relevant stakeholders for a particular set of issues. This lack of explanation of definition constitutes a core lack of transparency in the consultation process.

Governmental authorities state that they take account of stakeholders in the policy-making context as a means of increasing public participation in decision-making. This paper argues that whereas the idea of recognizing the stakeholder is presented as including voices in the policy process which might otherwise be excluded, the idea of the stakeholder is in itself inherently exclusive, because it suggests that there are some people who are not stakeholders.

The definition of stakeholders to include specific categories of person tends to suggest that the views of members of the named groups are more relevant than those of others who are

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not named.¹ Consultation documents and questionnaires do not explicitly address issues of stakeholder definition: they do not explain the processes adopted for defining relevant stakeholders, or the choice not to define the relevant stakeholders for a particular set of issues. A lack of transparency about who policy-makers consider to be key stakeholders in the policy process, and how they define such key stakeholders undermines the transparency of the consultation process generally.²

The paper concentrates on the construction of the stakeholder in the arena of financial regulation, because financial regulation presents special problems for the definition of stakeholders. Narratives are significant in the development of policy, and those who define the narratives can effectively influence policy.³ The narratives of financial regulation are usually

¹ The definition of stakeholders is complex. *See, e.g.*, EU Commission, Towards a Reinforced Culture of Consultation and Dialogue - General Principles and Minimum Standards for Consultation of Interested Parties by the Commission, p. 5 COM(2002) 704 (Dec. 11, 2002) (“the challenge of ensuring an adequate and equitable treatment of participants in consultation processes should not be underestimated. The Commission has underlined, in particular, its intention to “reduce the risk of the policy-makers just listening to one side of the argument or of particular groups getting privileged access[...].” This means that the target groups of relevance for a particular consultation need to be identified on the basis of clear criteria” (footnote omitted).)

² *Cf.* Carol Harlow, *Global Administrative Law: The Quest for Principles and Values*, 17 *Eur. J. Int’l L.* 187, 202 (2006) (“Here the Commission is disingenuous in pretending that decisions as to ‘which associations should be consulted and whose suggestions should be accepted, or in deciding which associational codes of conduct should pass muster, value judgments are not made’. A substantial administrative discretion with important political implications is concealed in these evaluations, which should be subjected to the controls of administrative law.”)

³ *Cf.* Anne Schneider & Mara Sidney, *What Is Next for Policy Design and Social Construction Theory?*, 37 *POLICY STUDIES J.* 103, 106 (2009) (“The policy design approach directs scholars to examine who constructs policy issues, and how they do so, such that policy actors and the public accept particular understandings as “real,” and how constructions of groups, problems and knowledge then manifest themselves and become institutionalized into policy designs, which subsequently reinforce and disseminate these constructions”.)

constructed by market participants.⁴ Whereas environmental groups can motivate large numbers of citizens to care about charismatic megafauna,⁵ issues of financial regulation do not always seem to be salient for citizens.⁶ Some narratives do help to make financial regulation salient to the public. For example, stories about predatory lending prompted states to enact statutes to control predatory lending.⁷ But financial regulation is complex and technical, and is often described in ways which limit the ability of non-experts to participate in discussions of the rules. After states legislated against predatory lending, rating agencies argued that the statutes would interfere with the securitization market and that this market was essential to enable consumers to borrow money to buy their homes.⁸ Until the global financial crisis the narrative of encouraging

⁴ See, e.g., Paul Krugman, *The Unwisdom of Elites*, N.Y. Times, A23 col. 4 (May 9, 2011) (the Great Recession brought on by a runaway financial sector, empowered by reckless deregulation. And who was responsible for that deregulation? Powerful people in Washington with close ties to the financial industry, that's who.)

⁵ See, e.g., Erin C. Barney, Joel J. Mintzes & Chiung-Fen Yen, Assessing Knowledge, Attitudes, and Behavior Toward Charismatic Megafauna: The Case of Dolphins, 36 *Journal of Environmental Education* 41 (2005); Jamie Lorimer, *International Conservation 'Volunteering' and the Geographies of Global Environmental Citizenship*, 29 *Political Geography* 311, 317 (2010) ("It is clear that the charisma of a small number of animals plays a key role in drawing volunteers into conservation."). The results of using this approach to motivate citizens have been criticized,. See, e.g., *id.* at 319 ("Aesthetic and iconic 'flagships' (be they elephants, children or celebrity advocates), appealing causes and the realities and perceptions of risk and cost all trigger and configure concern. The resources they draw in or deter make them matter more and more, perhaps at the expense of less fun, safe, touching or glamorous causes. In this political economy charisma might be the only thing that secures your future.")

⁶ But *cf.* Debit Interchange Rule Delayed (Mar. 31, 2011) at <http://financialreform.wolterskluwerlb.com/2011/03/debit-interchange-rule-delayed.html> (Noting more than 11,000 comments on .a proposed rule).

⁷ See, e.g., Baher Azmy, *Squaring the Predatory Lending Circle: A Case for States as Laboratories of Experimentation*, 57 *FLA. L. REV.* 295 (2005). See also, e.g., Kathleen C. Engel & Patricia A. McCoy, *A Tale of Three Markets: The Law and Economics of Predatory Lending*, 80 *TEX. L. REV.* 1255 (2001-2002) (analyzing the problem of predatory lending)

⁸ See, e.g., Azmy, *supra* note 7, at 316.

home ownership and preventing states from interfering with the securitization market seemed to prevail. After the crisis hit and led to a foreclosure crisis, a new narrative of securitization developed. The new narrative emphasized the ways in which the practice of securitization deviated from their theory. Securitization did not transfer credit risk from originators as proponents of securitization had argued. Commentators argued that rather than originating to distribute, securitizers had been in the business of originating and pretending to distribute.⁹ This new narrative made regulation of securitization more feasible.¹⁰ More generally, policy-makers began to question earlier habits of deference to arguments that the markets should be allowed to manage themselves.¹¹

Although financial regulation is sometimes politically salient, the details of rule-making are complex and technical. And when they seek views on proposals to change the details of financial regulation, policy-makers often define the relevant issues in technical terms. This means

⁹ C.A.E. Goodhart, *The Regulatory Response to the Financial Crisis*, *Journal of Financial Stability* 351, 356 (2008) (“the banking business strategy known as ‘originate and distribute’ should have been better re-entitled as ‘originate and pretend to distribute’. What surprised, and should have shocked, most of us was the extent to which banks transferred assets to vehicles closely related to themselves, conduits and SIVs of various kinds, to which they were bound, either by legal commitment or by reputational risk, to support whenever funding, or other, financial conditions become adverse.”)

¹⁰ *See, e.g.*, Department of the Treasury, Office of the Comptroller of the Currency, Federal Reserve System, Federal Deposit Insurance Corporation, Federal Housing Finance Agency, Securities & Exchange Commission, Department of Housing and Urban Development, Credit Risk Retention, 76 Fed. Reg. 24090 (Apr. 29, 2011). The attitude of the Supreme Court to pre-emption of state regulation of banks seemed to change between 2007 and 2009. Contrast *Watters v. Wachovia Bank* 550 U.S. 1 (2007) and *Cuomo v. Clearing House Association* 129 S. Ct. 2710 (2009).

¹¹ *See, e.g.*, FSA, *The Turner Review: A Regulatory Response to the Global Banking Crisis*, 49 (Mar. 2009) available at http://www.fsa.gov.uk/pubs/other/turner_review.pdf (“Turner Review”) (“An underlying assumption of financial regulation in the US, the UK and across the world, has been that financial innovation is by definition beneficial, since market discipline will winnow out any unnecessary or value destructive innovations. As a result, regulators have not considered it their role to judge the value of different financial products, and they have in general avoided direct product regulation, certainly in wholesale markets with sophisticated investors.”)

that the real stakeholders seem to be the people and organizations that have relevant expertise. Moreover, only specific types of knowledge are treated as relevant expertise.¹² Even if the general public wishes to express views on proposed financial rules,¹³ citizens may be uncertain as to whether their views would be considered to be relevant and how their responses would be processed.¹⁴ Policy-makers do not spell out in advance how they propose to weigh different types of contribution to any consultation process, nor do they necessarily explain afterwards how they did weigh different contributions. In addition, the views of the public are most likely to be seen as relevant as such when they relate to consumers' vulnerability and problems of understanding financial products, and this tends to undermine consumers' credibility as commentators on financial regulation generally.

¹² *Cf. id.* at 45 (“In the past, an important school of thought has argued that market discipline can play a key role in incentivising banks to constrain capital and liquidity risks....But a strong case can be made that the events of the last five years have illustrated the inadequacy of market discipline: indeed, they suggest that in some ways market prices and market pressures may have played positively harmful roles.”)

¹³ *Cf. Robin Gauld, Shaun Goldfinch & Simon Horsburgh, Do they want it? Do they use it? The ‘Demand-Side’ of e-Government in Australia and New Zealand, 27 GOVERNMENT INFORMATION QUARTERLY 177, 184 (2010)* (“Much of the literature on e-government suffers from an overly technological focus. It is assumed that once the correct technology is developed and in place, and citizens given access, benefits will be delivered in terms of reduced costs and technical efficiency, greater access and greater accountability and transparency, the transformation of government operations, and even greater ‘e-participation’ and ‘e-democracy’... The downsides and limitations of e-government are often downplayed or ignored altogether.”)

¹⁴ For example, the SEC stated that “Staff will try to meet with any interested parties seeking a meeting. When the number of requests exceeds availability, the staff will seek out parties with varying viewpoints. Staff may have to limit the number of meetings with similarly situated parties and will limit multiple meetings with the same party.”Sec. & Exch. Comm’n, Press Release, SEC Chairman Schapiro Announces Open Process for Regulatory Reform Rulemaking, Jul. 27, 2010 at <http://www.sec.gov/news/press/2010/2010-135.htm>.

Stakeholders in Consultation

Consultation¹⁵ reflects a general expressed commitment to transparency and accountability,¹⁶ but governments and agencies communicate to the public about consultations in very different ways. There are differences of approach between different geographic jurisdictions and also within jurisdictions.¹⁷ One set of variations, and the one on which this paper focuses, relates to the definition or non-definition of relevant stakeholders. US notice and comment rule-making is open to all, at least as a formal matter. Agencies publish notices of proposed rule-making in the Federal Register, and invite comments generally without specifying who they consider to be stakeholders. However, long before an agency proposes rules as a formal matter it may meet with interested parties, and such meetings can help to frame the regulatory agenda. Even where stakeholders are not explicitly defined in consultation documents and notices of proposed rule-making, agencies responsible for the development of policy have made determinations about which groups they need to involve in the policy-development process. A

¹⁵ See, e.g., Caroline Bradley, *Consultation and Legitimacy in Transnational Standard-Setting* (forthcoming MINN. J. INT'L L. (2011))

¹⁶ See, e.g., Sec. & Exch. Comm'n Press Release, *supra* note [14](#) ("Under a new process, the public will be able to comment before the agency even proposes its regulatory reform rules and amendments.... The new process goes well beyond what is legally required and will provide expanded opportunity for public comment and greater transparency and accountability. The SEC also expects to hold public hearings on selected topics."). See also, e.g., Memorandum for the Heads of Executive Departments and Agencies, Transparency and Open Government, 74 Fed. Reg. 4685 (Jan. 26, 2009); Memorandum for the Heads of Executive Departments and Agencies, Open Government Directive (Dec. 8, 2009) at http://www.whitehouse.gov/sites/default/files/omb/assets/memoranda_2010/m10-06.pdf (Open Government Directive); EU Commission, *supra* note [1](#), at 5 ("good consultation serves a dual purpose by helping to improve the quality of the policy outcome and at the same time enhancing the involvement of interested parties and the public at large. A further advantage is that transparent and coherent consultation processes run by the Commission not only allow the general public to be more involved, they also give the legislature greater scope for scrutinising the Commission's activities.")

¹⁷ Comparing the practice of consultation in different jurisdictions is a complex exercise because the details of the rules which apply to different types of consultation vary enormously, as do the constitutional and institutional structures within which consultation is embedded.

failure explicitly to identify these implicit stakeholders undermines transparency. Even when policy-makers do identify stakeholders in the proposals they put forward they do not explain the methods whereby they identified those stakeholders, and this failure also impedes transparency.¹⁸

The US has recently moved to increase governmental transparency. The Open Government Directive does not use the term “stakeholder” but states that “[p]articipation allows members of the public to contribute ideas and expertise so that their government can make policies with the benefit of information that is widely dispersed in society.”¹⁹ Nevertheless, the implementation of the Directive involves the use of the stakeholder concept. For example, the Treasury’s Open Government Plan refers to communication with “public stakeholders.”²⁰ For the Treasury this includes an “outreach effort” by FinCEN with “representatives from a variety of industries that fall under BSA regulatory requirements.”²¹ The plan also refers to “the communication strategy for the public, open government advocacy groups, and key

¹⁸ On the distinction between transparency and effective communication, *see, e.g.*, Onora O’Neill, *Ethics for Communication?* 17 EUR. J. PHIL. 167 (2009). *Cf.* International Association for Public Participation, IAP2 Core Values of Public Participation, (2007) at <http://www.iap2.org/associations/4748/files/CoreValues.pdf>.

¹⁹ Open Government Directive, *supra* note 16, at 1. *Cf.* OMB, Memorandum for the Heads of Executive Departments and Agencies M-11-19, Retrospective Analysis of Existing Significant Regulations (Apr. 25, 2011) at <http://www.whitehouse.gov/sites/default/files/omb/memoranda/2011/m11-19.pdf> (“Because members of the public are likely to have useful information and perspectives, agencies should promote public consultation about the plans. Agencies are encouraged to use the first thirty days after releasing their plans to engage in such public consultation.”); Department of the Treasury, Reducing Regulatory Burden; Retrospective Review Under E.O. 13563 76 Fed. Reg. 17572, 17572 (Mar. 30, 2011) (“How can Treasury improve public outreach and increase public participation in the rulemaking process?”)

²⁰ Department of the Treasury, Open Government Plan, 7 (May 2010) (revised) at http://www.treasury.gov/open/Documents/open_government_plan.pdf.

²¹ *Id.* (“FinCEN has concluded its meetings with some of the largest depository institutions and money services businesses in the United States, and is continuing its most recent outreach phase with smaller depository institutions.”)

stakeholders.”²² This language implies a distinction between these three groups: the public and “key stakeholders” are not identical.

After executive departments and agencies of the US Government began to develop their open government plans, the Administration initiated a broad regulatory review which required agencies to ensure public participation in the development of regulations. The Executive Order referred specifically to stakeholders.²³ Thus the US has adopted the language of stakeholding as a component of its regulatory process, although not so far as enthusiastically as other jurisdictions have done.²⁴

In the aftermath of the global financial crisis, legislators and regulators charged with developing new rules and regulations have sought comments from the public about the new rules. For example, in the US after the enactment of the Dodd-Frank Wall Street Reform and Consumer Protection Act²⁵ the SEC announced measures to allow the public to make comments about how the agency should go about making rules, rather than merely responding to the SEC’s specific regulatory proposals.²⁶ The Chairman of the SEC, Mary Schapiro stated that:

"We recognize that the process of establishing regulations works best when all stakeholders are engaged and contribute their combined talents and

²² *Id.* at 8.

²³ Executive Order 13563 of January 18, 2011, Improving Regulation and Regulatory Review, 76 Fed. Reg. 3821, 3821 (Jan 21, 2011) (“Regulations shall be adopted through a process that involves public participation. To that end, regulations shall be based, to the extent feasible and consistent with law, on the open exchange of information and perspectives among State, local, and tribal officials, experts in relevant disciplines, affected stakeholders in the private sector, and the public as a whole.”)

²⁴ *See, e.g.*, EU Commission Communication, Smart Regulation in the European Union, 2 COM(2010) 543 (Oct. 8, 2010) (“The better regulation agenda has already led to a significant change in how the Commission makes policy and proposes to regulate. Stakeholder consultations and impact assessments are now essential parts of the policy making process. They have increased transparency and accountability, and promoted evidence-based policy making.”)

²⁵ Pub. L. 111-203 (Jul. 21, 2010).

²⁶ *See supra* note [14](#).

experiences.”²⁷

At the same time, the SEC solicited public comments in the context of a study of broker-dealer regulation it was mandated to carry out under the statute.²⁸ The online comment forms invited respondents to provide personal information, including information about any professional affiliations,²⁹ but did not require respondents to identify themselves as representatives of any particular interest group or type of group.³⁰ In contrast, the UK Government’s Consultation on Phasing out the Default Retirement Age, also published in July of 2010, required respondents to identify to which of a number of different categories they belonged.³¹ HM Treasury’s

²⁷ *Id.* See also the web page for Public Comments on SEC Regulatory Initiatives Under the Dodd-Frank Act at <http://www.sec.gov/spotlight/regreformcomments.shtml>.

²⁸ Sec. & Exch. Comm’n, Study Regarding Obligations of Brokers, Dealers, and Investment Advisers, Request for Comment (Jul. 27, 2010) at <http://www.sec.gov/rules/other/2010/34-62577.pdf>.

²⁹ *See, e.g.*, the form at http://www.sec.gov/cgi-bin/ruling-comments?ruling=4-606&rule_path=/comments/4-606&file_number=4-606&action=Show_Form&title=Study%20Regarding%20Obligations%20of%20Brokers%2C%20Dealers%2C%20and%20Investment%20Advisers.

³⁰ The study was published in January 2011. Sec. & Exch. Comm’n, Study on Investment Advisers and Broker-Dealers (Jan. 2011) at <http://www.sec.gov/news/studies/2011/913studyfinal.pdf> (“SEC Investment Adviser Study”). See also Commissioners Kathleen L. Casey and Troy A. Paredes, Statement Regarding Study On Investment Advisers And Broker-Dealers (Jan. 21, 2011) at <http://www.sec.gov/news/speech/2011/spch012211klctap.htm>.

³¹ Department of Business, Innovation and Skills & Department for Work and Pensions, Phasing out the Default Retirement Age (Jul. 2010) at <http://www.bis.gov.uk/assets/biscore/employment-matters/docs/p/10-1047-default-retirement-age-consultation.pdf>. The specified categories were: “Business representative organisation/trade body; Central government; Charity or social enterprise; Individual; Large business (over 250 staff); Legal representative; Local government; Medium business (50 to 250 staff); Micro business (up to 9 staff); Small business (10 to 49 staff); Trade union or staff association; Other (please describe)”. *Id.* at 22. *See also, e.g.*, the Consultation response form on The Future of Narrative Reporting, (Aug. 2010) available from <http://bis.gov.uk/assets/biscore/business-law/docs/n/10-1057rf-future-narrative-reporting-consult>

consultation on financial regulation did not require such categorization, but did ask respondents to state whether they were responding as an individual or on behalf of an organization and also stated that the Government would be engaging “directly with relevant stakeholders” before the consultation’s closing date.³² Consultations by the EU Commission similarly invite respondents to specify the capacity in which they are responding to consultations. For example, the August 2010 consultation on concessions has separate questionnaires for contracting authorities, social partners and the business community,³³ and the July 2010 consultation on a European Contract Law separates respondents into groups of citizens, organizations and public authorities.³⁴ The Commission’s July 2010 consultation on insurance guarantee schemes sought contributions in particular from “market participants, national governments and national competent authorities”

[ation-response.doc](#) (Inviting respondents to identify themselves as a Quoted company; Other company; Investor or investment manager; Business representative organisation; Investor representative organisation; Non governmental organisation (NGO); Trade Union; Lawyer or accountant or Other (e.g. consultant or private individual).)

³² HM Treasury, *A New Approach to Financial Regulation: Judgement, Focus and Stability*, 59 Cm. 7874 (Jul. 2010) at http://www.hm-treasury.gov.uk/d/consult_financial_regulation_condoc.pdf. The document does not specify who the Government considers to be the “relevant stakeholders”. The Government published a summary of responses to the consultation in November 2010, noting that Government representatives had met with a range of stakeholders. HM Treasury, *A New Approach to Financial Regulation: Summary of Consultation Responses*, 3 (Nov. 2010) at <http://www.hm-treasury.gov.uk/d/summaryofcondocresponses241110.pdf>. (“During the consultation period, Treasury Ministers and their officials met a wide range of interested parties to discuss the proposals, including a number of bilateral meetings and workshops with stakeholders. Discussions with international counterparts were also held.”).

³³ See http://ec.europa.eu/internal_market/consultations/2010/concessions_en.htm.

³⁴ See http://ec.europa.eu/justice_home/news/consulting_public/news_consulting_0052_en.htm. See also European Commission, *Green Paper from the Commission on Policy Options for Progress Towards a European Contract Law for Consumers and Businesses*, COM (2010) 348 (Jul. 1, 2010) at http://ec.europa.eu/justice_home/news/consulting_public/0052/consultation_questionnaire_en.pdf.

although it stated that contributions were welcomed from all citizens and organizations.³⁵

That public consultations about financial regulation differ in the extent to which they actively seek input from a broad range of members of the public is inevitable. Members of the public are likely to have less knowledge and experience about the infrastructure of financial markets³⁶ or credit risk retention³⁷ than about their own experiences of making investment and borrowing decisions.³⁸ Indeed, the need to improve financial literacy is one issue on which regulators must focus.³⁹ The financial crisis illustrates that we all have an interest in the regulation of the financial markets. It may be unrealistic to imagine general participation in discussions of how that regulation should be constructed and implemented, but that is what policy-makers seem to promise. And it is sometimes difficult to reconcile the grand public rhetoric about transparency and the importance of public participation in governance with specific examples of consultations and requests for comments.

In some cases issues of financial regulation clearly involve matters of concern to consumers of financial services, and even if the relevant policy-makers do not identify consumers

³⁵ See http://ec.europa.eu/internal_market/consultations/2010/whitepaper-on-igs_en.htm. See also European Commission, White Paper on Insurance Guarantee Schemes, COM (2010) 370 (Jul. 12, 2010) at <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2010:0370:FIN:EN:PDF>.

³⁶ See, e.g., Committee on Payment and Settlement Systems, Technical Committee of the International Organization of Securities Commissions, Principles for Financial Market Infrastructures: Consultative Report (Mar. 2011) at <http://www.bis.org/publ/cpss94.pdf>.

³⁷ See, e.g., Credit Risk Retention proposal, *supra* note 10, at 24090 (Inviting comments from “interested parties.”).

³⁸ See, e.g., the SEC Investment Adviser Study, *supra* note 30, and the request for comments preceding the study, *supra* note 28.

³⁹ See, e.g., Sec. & Exch. Comm’n, Comment Request on Existing Private and Public Efforts to Educate Investors, 76 Fed. Reg. 22740, 22741 (Apr. 22, 2011) (“All interested parties, including those organizing or operating investor education programs and program attendees and participants, are invited to submit their views.”) Cf. OECD, Improving Financial Literacy: Analysis of Issues and Policies (2005).

as stakeholders they will make their views known. For example, the SEC's recent study of the regulation of brokers and investment advisers was mandated by the Dodd-Frank Act, which required the SEC to consider legal protections for retail customers with respect to personalized investment advice.⁴⁰ The SEC was to consider a number of issues, including "[w]hether retail customers understand or are confused by the differences in the standards of care that apply to broker-dealers and investment advisers."⁴¹ The Investment Adviser Study recommends that the fiduciary standard which currently applies to investment advisers should also apply to broker-dealers when they provide investment advice about securities to retail customers.⁴²

The SEC received over 3500 comment letters in response to its request for comments.⁴³ In addition staff of the SEC "met with interested parties representing investors, broker-dealers, investment advisers, other representatives of the financial services industry, academics, state securities regulators, the North American Securities Administrator Association ("NASAA"), and the Financial Industry Regulatory Authority ("FINRA"), which serves as a self-regulatory organization ("SRO") for broker-dealers."⁴⁴ The Investment Adviser Study states that:

Many retail investors and investor advocates submitted comments stating that retail investors do not understand the differences between investment advisers and broker-dealers or the standards of care applicable to broker-dealers and investment advisers. Many find the standards of care confusing, and are uncertain about the meaning of the various titles and designations used by investment advisers and broker-dealers. Many expect that both investment advisers and broker-dealers are obligated to act in the investors' best interests.⁴⁵

⁴⁰ SEC Investment Adviser Study, *supra* note 30 at i-ii.

⁴¹ *Id.* at i.

⁴² *Id.* The report describes this as a "uniform fiduciary standard." *Id.*

⁴³ *Id.* at ii.

⁴⁴ *Id.*

⁴⁵ *Id.* at v. Comments are available at <http://www.sec.gov/comments/4-606/4-606.shtml>.

The Study cites comment letters from sixteen investors and two investor advocates.⁴⁶ Emphasizing these comments in the Study shows that the SEC staff treated the views of these investors and investor advocates seriously, not surprisingly given the SEC's mandate under the statute. The conclusions expressed in the Study do address the issue raised by the individual comments that some consumers of financial services do not appreciate that different providers of advice are subject to different regulatory requirements. But the conclusion the Study draws, that the investment adviser standard should apply to all providers of personalized investment advice to retail customers, is not compelled by the investors' comments, and others have criticized the Study, arguing that the SEC did not research thoroughly enough the implications of the proposed rule change.⁴⁷

In some cases the individual commenters' responses seem to have been prompted by news articles,⁴⁸ suggesting that they were not actively engaged in looking for opportunities to express their views on financial regulation. The content of their responses tends to underline the

⁴⁶ See Comments of David Certner, Legislative Counsel and Legislative Policy Director, American Association of Retired Persons (Aug. 30, 2010) at <http://www.sec.gov/comments/4-606/4606-2549.htm>; Comments of Barbara Roper, Director of Investor Protection, Consumer Federation of America (Aug. 30, 2010) at <http://www.sec.gov/comments/4-606/4606-2448.pdf> (CFA Submission).

⁴⁷ See, e.g., Statement of Commissioners Casey and Paredes, *supra* note 30 ("the Study does not identify whether retail investors are systematically being harmed or disadvantaged under one regulatory regime as compared to the other and, therefore, the Study lacks a basis to reasonably conclude that a uniform standard or harmonization would enhance investor protection. A stronger analytical and empirical foundation than provided by the Study is required before regulatory steps are taken that would revamp how broker-dealers and investment advisers are regulated.")

⁴⁸ See, e.g., Comments of Elizabeth Marion, (Aug. 31, 2010) cited in the SEC Investment Adviser Study, *supra* note 30 at footnote 448 on page 94. The letter is also available at <http://www.sec.gov/comments/4-606/4606-2672.htm> (the online comments file describes this respondent's name as Elizabeth Manion). See also, e.g., CFA Submission, *supra* note 46 ("In an effort to encourage more investor response, CFA issued a news release to personal finance writers in mid-August designed to prompt them to write columns and articles encouraging investors to make their voices heard.")

idea that some consumers of financial services are relatively uninformed and vulnerable to being abused by their advisers.⁴⁹ These characteristics do not make consumers credible generally as commentators on proposals for rules of financial regulation.⁵⁰ Thus even where consumers are most clearly among the relevant stakeholders with respect to regulatory proposals the ways in which they participate in the regulatory process undermine their ability to influence the way in which the rules are developed. The style, form, and content of the submissions of the AARP and of the Consumers' Federation of America⁵¹ are dramatically different from those of the individual commenters, and comparable to those written by other responding organizations.

The example of the preparation of this study, and, in particular the CFA's comments, suggest that if the SEC wants the reality to match up to its rhetoric of public consultation it needs to develop a more sophisticated approach to incorporating the information investors have about how its rules operate in developing effective regulation. The CFA's submission suggests that the SEC could have done more to reach out to individual investors in preparing for the Study.⁵² The CFA suggests using different techniques to generate public input, such as holding town meetings, and that the SEC could try to focus on where investors would be able to have the most relevant input:

⁴⁹ *See, e.g., id.*

⁵⁰ Contrasting with this image of the uninformed, vulnerable consumer is the recognition that communities have put enormous efforts into resolving the foreclosure crisis. *See, e.g.,* Governor Elizabeth A. Duke, Community Voices: Promising Practices for Neighborhood Stabilization, Speech at the 2011 Federal Reserve Community Affairs Research Conference, Arlington, Virginia (Apr. 28, 2011) at <http://www.federalreserve.gov/newsevents/speech/duke20110428a.htm>.

⁵¹ *See supra* note [46](#).

⁵² CFA Submission, *supra* note [46](#) (“A preliminary review of comment letters submitted through the beginning of last week suggests that virtually all letters submitted at that time had come from members of the industry. While the comment period had one week remaining when this review was conducted, the results suggest that more needs to be done to encourage greater input from investors. We therefore urge the Commission to take additional steps to reach out to average investors.”)

Another option would be for the Commission to release an appeal for comments from Chairman Schapiro, sent to newspapers throughout the country. Such an appeal could and should hone in on the issues where investors are most likely to have relevant input: whether they understand the differences between different types of investment professionals, what they expect from a financial adviser, what protections they believe would be beneficial, and what their experience has been in shopping for and working with investment professionals. Investors need to understand that, even if they lack technical expertise in the issues covered by the study, they have a view that deserves consideration.⁵³

It is particularly striking to note the CFA's critique of the SEC's approach to obtaining input from the public in a context where Congress specifically instructed the SEC to study "[w]hether retail customers understand or are confused by the differences in the standards of care that apply to broker-dealers and investment advisers."⁵⁴ In other contexts the SEC is even less likely to work to obtain useful input from investors.

The UK Government's consultation on a New Approach to Financial Regulation⁵⁵ was a broader consultation about financial regulation than the SEC's work on its Investment Adviser Study, and, as noted above, the Government suggested that it would engage with "relevant stakeholders", although it also invited responses generally.⁵⁶ In describing the results of the consultation, the Government stated that it had received "[a]round 220 formal written responses

⁵³ *Id.*

⁵⁴ *See supra* at page [12](#).

⁵⁵ *See supra* note [32](#). The UK Government also established an Independent Commission on Banking which published an initial report in April 2011. Independent Commission on Banking, Interim Report: Consultation on Reform Options (Apr. 2011) at <http://s3-eu-west-1.amazonaws.com/htcdn/Interim-Report-110411.pdf>.

⁵⁶ A New Approach to Financial Regulation, *supra* note [32](#), at 59 ("Responses are requested by 18 October 2010. The Government will also engage directly with relevant stakeholders ahead of this date")

... from a diverse range of stakeholder groups.”⁵⁷ The Summary of Responses ascribes responses to vague groups of commenters, referring to “a number of respondents,” “the majority of respondents,” or “the overwhelming majority of respondents,” and “near-universal consensus.”⁵⁸

At times views are ascribed to groups with particular characteristics. For example:

The majority of respondents, including almost all financial services sector respondents, stressed the importance of accountability and transparency for the PRA, the CPMA and the FPC, including through appropriate engagement with regulated firms.⁵⁹

Although the Summary states that it is important to protect consumers, consumer protection is not the primary objective,⁶⁰ and the Summary is drafted to reassure the regulated population that their interests will be considered:

The Government also notes that the PRA and CPMA will operate under the usual obligation placed on public bodies to behave reasonably and in the public interest; this obligation should provide industry and other stakeholders with comfort that the new authorities will consider the impact of their actions on those they regulate.⁶¹

⁵⁷ A New Approach to Financial Regulation: Summary of Consultation Responses, *supra* note 32, at 4. The respondents (whose responses are public) are listed at pages 19-24 of the Summary of Responses. The responses are also available at http://www.hm-treasury.gov.uk/consult_financial_regulation.htm. The web page provides links to seven separate pdf files representing comments by respondents organized alphabetically. While it is possible to navigate around each document this method of organizing responses does not seem to be designed to maximize transparency.

⁵⁸ *Id.* at 5.

⁵⁹ *Id.*

⁶⁰ *See, e.g.*, A New Approach to Financial Regulation: Summary of Consultation Responses, *supra* note 32, at 7 (“The description of the CPMA as a consumer champion was welcomed by many respondents, though many also noted that this should not compromise the regulator’s independence or lead to consumer protection taking precedence over other factors.”)

⁶¹ *Id.* at 8.

The Summary document notes some concern that “the governance structure proposed could lead to a concentration of power within the Bank of England.”⁶² The document does specifically note some comments of consumer groups.⁶³ But reading the Summary document does not give much of a hint of which specific groups of stakeholders held which views, and, although the individual responses are available on the Treasury’s website, they are not organized to be easy to review.⁶⁴ The Government’s grand claims to be committed to transparency in the development of the new rules⁶⁵ are not borne out by the details of its work.

The UK Treasury’s initial consultation on the New Approach to Financial Regulation was followed in early 2011 by a more detailed report and consultation.⁶⁶ The new consultation document explicitly links to the earlier consultation and to the Summary document, presenting the new document as the product of the earlier consultation, and of the Government’s work in

⁶² *Id.* at 14. This presumably involves a recognition that there was a time when people said that the City of London was regulated by the Governor of the Bank of England’s eyebrows. See, e.g., Adam Tickell, *Creative Finance and the Local State: the Hammersmith and Fulham Swaps Affair*, 17 *Political Geography* 865, 876 (1998) (“Until the 1970s, the London financial markets operated on a largely informal basis where, with very few exceptions, verbal agreements were cast in stone and the probity of the markets was guaranteed by the fabled power of the Governor of the Bank of England’s eyebrow.”)

⁶³ See, e.g., A New Approach to Financial Regulation: Summary of Consultation Responses, *supra* note 32, at 15 (“Some consumer representatives argued for greater transparency, specifically in the context of the CPMA’s decision-making and maintaining an open dialogue with consumer groups.”)

⁶⁴ See, e.g., *supra* note 57.

⁶⁵ See, e.g., A New Approach to Financial Regulation: Summary of Consultation Responses, *supra* note 32, at 4 (“The Government remains fully committed to an open and transparent policy-making process.”)

⁶⁶ HM Treasury, A New Approach to Financial Regulation: Building a Stronger System, Cm. 8012 (Feb. 2011) at http://www.hm-treasury.gov.uk/d/consult_newfinancial_regulation170211.pdf.

response to the results of that consultation.⁶⁷ But in the new document the Government explains its views on transparency and financial regulation in a new way:

... consistent with its wider agenda on the reform of public institutions, the Government is fully committed to the accountability and transparency of the new regulatory institutions. The location of responsibilities within independent, expert institutions is a model of public administration which is well suited to technical issues – such as financial regulation – for which certainty, long-term focus and a degree of insulation from political influence is important. However, the model also depends on there being clear accountability for performance, supported by transparency and, where appropriate, engagement with affected segments of society.⁶⁸

The 2011 version of the new approach contains a particular vision of the role of the consumer of financial services: consumers are responsible for their own decisions,⁶⁹ consumers

⁶⁷ *See, e.g., id.* at 6 (“The November summary response set out the Government’s emerging thinking on each of these themes. Based on the work carried out by the Treasury, Bank and FSA over the last seven months, the Government is now able to provide far more detailed and specific policy responses in each of these areas. The remainder of this introduction highlights some of the main developments since the July document was published.”)

⁶⁸ *Id.* at 9. The reference to the insulation of financial regulation from politics is somewhat ironic as the impetus to reform financial regulation is largely political. *See, e.g., id.* at 3 (“The Government recognises that steps must also be taken to ensure that financial firms are never again allowed to take on risks that are so significant and so poorly understood, resulting in such severe economic consequences for businesses, households and individuals. That is why the Coalition Government made the reform of UK financial regulation, and the replacement of the flawed system introduced by the previous administration, one of its key priorities on taking office in May 2010.”)

⁶⁹ The Consultation document proposes that one of the basic principles of the new regulatory regime is to be “the principle that consumers of financial services are ultimately responsible for their own decisions.” *Id.* at 8.

benefit from competition between financial services providers,⁷⁰ but sometimes consumers need redress and compensation.⁷¹ These assumptions about consumer responsibility and the connection between competition in markets and consumer benefit are not uncontroversial.⁷² It is unclear from the document to what extent the Government planned to solicit the views of consumers and consumer groups in the consultation. In order to move ahead with the legislative process the consultation period is only eight weeks long, although the document emphasizes that this is not an issue as there will be future opportunities for stakeholders to comment on the proposals.⁷³ The document also states that the Government will

⁷⁰ *Id.* at 8 (“Competition will be an important new feature of the regulatory remit, incorporated in a way that goes significantly beyond the current FSMA framework. This will provide a significant step forward in terms of recognising the importance of competition in delivering good outcomes for consumers of financial services.”) The UK Government has also recently proposed changes to competition law. *See, e.g.*, Department for Business, Innovation and Skills, A Competition Regime for Growth: A Consultation on Options for Reform (Mar. 2011) at <http://www.bis.gov.uk/assets/biscore/consumer-issues/docs/c/11-657-competition-regime-for-growth-consultation.pdf>. *See also, e.g.*, Department for Business, Innovation and Skills & Cabinet Office, Better Choices, Better Deals: Consumers Powering Growth, (Apr. 2011) at <http://www.cabinetoffice.gov.uk/sites/default/files/resources/better-choices-better-deals.pdf>.

⁷¹ Building a Stronger System, *supra* note 66 at 9 (“Finally, the Government also recognises that redress and compensation have a part to play in the regulatory system, to provide consumers – particularly retail customers – with appropriate mechanisms to protect them if things go wrong.”)

⁷² *See, e.g.*, OFT, Consumer Behavioural Biases in Competition, A Report by Steffen Huck, Jidong Zhou, and London Economics Charlotte Duke, 6 (May 2011) at http://www.of.gov.uk/shared_of/research/OFT1324.pdf (“Perhaps the most striking result of the literature so far is that increasing competition through fostering entry of more firms may not always make consumers better off and in specific circumstances may even make consumers worse off.”)

⁷³ Building a Stronger System, *supra* note 66 at 13 (“the Government will consult on the proposals contained in this document for eight weeks, before publishing a draft Bill in the spring. This draft Bill will then be subject to full, formal pre-legislative scrutiny....The Government recognises that the consultation period for this policy document is shorter than normal. This expedited process is necessary to enable formal pre-legislative scrutiny to be conducted, without

proactively seek the views of respondents in a structured way, and to engage in dialogue and discussion so that policy proposals continue to develop through the consultation period and beyond.⁷⁴

The 2010 New Approach Consultation did not identify the relevant stakeholders, but the 2011 consultation does state that:

the Government will ensure that the momentum behind this crucial reform programme is maintained, while maximising the opportunities for industry, consumer groups, and other interested parties, to engage constructively with the process.⁷⁵

The 2011 consultation document also describes the general public as “the ultimate stakeholder in the regulatory system.”⁷⁶ The document as a whole makes a number of quite vague and indefinite references to different stakeholders without any indication of what precise steps the Government proposes to take to include the views of the different groups in the process for development of draft legislation. It is not a model of transparency in this respect. But the consultation document suggests that the Government sees input from consumers as relevant only to the evidently consumer aspects of regulation. For example, the Government does not propose that the new PRA should have a consumer panel.⁷⁷ The public will have the right to be consulted annually on

significantly extending the timetable for reform. Pre-legislative scrutiny will, in any case, provide a significant additional opportunity for stakeholders to provide input into the development of the legislative framework.”)

⁷⁴ *Id.*

⁷⁵ *Id.* at 14.

⁷⁶ *Id.* at 55.

⁷⁷ *Id.* at 57-8 (“A number of respondents to the July consultation suggested that the PRA should be required to maintain a standing consumer panel, for the purposes of seeking views from consumers about the effectiveness of its regulation. While consumer issues will be integral to the new regulatory structure – particularly with the creation of a dedicated new consumer protection regulator – on reflection the Government does not think that it will be necessary to retain the consumer panel for the PRA. The PRA will be focused exclusively on prudential

the work of the PRA but there will be no consumer panel to focus on its work on an ongoing basis.⁷⁸ Readers of the document have to wade through to page 58 of the document to discover this fact. The drafters of the consultation document assume, rather than explain, that it is appropriate to limit consultation of consumers to the areas where their interventions are deemed appropriate by those in charge. But the ability of market participants to express their opinions on the activities of the PRA and the FCA is not to be limited in the same way.⁷⁹ And in some cases of conflict between the two bodies the Government proposes that the PRA should prevail.⁸⁰

The examples of the SEC's development of its Investment Adviser Study and the UK Government's work on its new approach to financial regulation both illustrate that policy-makers who focus on financial regulation tend to distinguish between areas of financial regulation which relate to consumer protection and other areas. They are more likely to seek comments from consumers on issues of consumer protection than on other issues of financial regulation. But they do not always make as much effort as they might to ensure consumer feedback even with respect to issues of consumer protection.

That policy-makers who focus on financial regulation treat financial institutions and other market participants as the important stakeholders in the development of financial regulation is not new. However, the SEC's and the UK Government's limited efforts to engage consumers described above are inconsistent with their own broad, general, and very visible, statements about

issues. Where the PRA believes that its decisions will have a material impact on consumers, it will be required to consult the FCA to take advantage of its expertise... the FCA will be required to maintain a consumer panel, consistent with its consumer protection role.”)

⁷⁸ *Id.* at 58.

⁷⁹ *Id.* at 66-7 (“The Government will therefore legislate for Practitioner, Smaller Business Practitioner, Markets and Consumer Panels for the FCA.”)

⁸⁰ *Id.* at 85 (“However, where the PRA and FCA cannot agree an appropriate course of action, the Government considers that it is necessary to enable the PRA to prevent the FCA from taking actions where it considers that they are likely to lead to the disorderly failure of a firm or wider financial instability (on which the PRA may consult the FPC). This recognises the fact that the PRA will be best placed to make this assessment and thereby avoid outcomes that would be harmful to both regulators’ objectives.”)

the importance of transparency and public consultation.⁸¹

Defining Stakeholders Transparently

In the examples above the policy-makers involved did not make significant efforts to be transparent about how they planned to engage with stakeholders. They did not specify clearly which stakeholders they planned to consult about which issues, nor precisely how they planned to do so. They did not explain what tools of stakeholder analysis they employed in developing their consultations. And they did not describe the results of their consultations in ways which made it clear who said what and how much attention the policy-makers had paid to the details of what they said.

This is not to suggest that the issue of how to defining the stakeholders with respect to any policy initiative is anything other than a complex problem.⁸² Different stakeholders likely have different views about what constitutes effective participation.⁸³ The policy-maker may have a number of different objectives in mind in making the definitional decision. Some consultations

⁸¹ Cf. B. Guy Peters, Jon Pierre & Tiina Randma-Liiv, *Global Financial Crisis, Public Administration and Governance: Do New Problems Require New Solutions?*, 11 PUBLIC ORGANIZ. REV. 13, 18 (2011) (“managing a crisis also requires gaining consensus or at least acquiescence across the society and decentralization may be a useful strategy for producing that legitimacy for the proposed changes. If governments have to undertake a range of novel and perhaps extreme policy initiatives then they may be well advised to involve stakeholders and the general public to the greatest extent possible.”)

⁸² Cf. Paul Dragos Aligica, *Institutional and Stakeholder Mapping: Frameworks for Policy Analysis and Institutional Change*, 6 PUBLIC ORGANIZ. REV. 79 (2006)

⁸³ Cf. Maureen M. Berner, Justin M. Amos & Ricardo S. Morse, *What Constitutes Effective Citizen Participation in Local Government? Views from City Stakeholders*, 35 Public Admin Quarterly 128, 129 (2011) (“Arguments in favor of citizen participation are rooted in normative theory, and as a result, discussions of what constitutes “effective” participation are likewise normatively-based. Yet we should be equally (if not more) concerned with how the stakeholders of participation— practitioners, elected officials, and citizens — understand effective citizen participation.”)

are not really consultations at all, but are designed to persuade the public.⁸⁴ One objective may be to ensure that the consultation process is as open and transparent as possible; another may be to ensure that those whose interests are affected by a policy proposal are included in the consultation, another may be to ensure that those who have relevant expertise are encouraged to share that expertise with the policy-maker, and yet another may be to ensure that those whose involvement is critical to the success of the initiative are involved and encouraged to make it succeed.

These objectives could be characterized as prioritizing good government, good policy,⁸⁵ or successful policy.⁸⁶ But although any or all of these objectives could be justifiable in some circumstances, they may also have problems. A policy-maker focused on achieving a particular result may approach consultation from the perspective of defining the issues, and the relevant stakeholders, in order to achieve the desired result. A policy-maker focused on producing good, evidence-based policy, may define the issues and the relevant stakeholders in a way that is not conducive to identifying the best policy options because of her own biases. A policy-maker focused on good government may focus so intensely on the issues of managing and processing responses that she loses sight of the real issues. And this may be a particular problem if the management and processing of the consultation is treated as an issue for technical experts in programming rather than those who have knowledge of the issue area.

⁸⁴ *Cf.* Resignation of Professor Brian Wynne from the Steering Group of the Food Standards Agency's public dialogue 'Food: the use of GM' (Jun. 2, 2010) at http://www.lancs.ac.uk/fass/doc_library/cesagen/FSAResignationpressreleaseBW.pdf (Quoting Professor Wynne as saying that the UK's Food Standards Agency "appears not to understand the socio-political as well as scientific fabric of such issues, and is thus unable to recognise its own social and political biases and confusions when doing what it calls public dialogue, and yet misrepresenting itself as following only "sound science."*)

⁸⁵ A policy-maker could be trying to develop good policy even if the policy-maker has an excessively limited view of what evidence is relevant to the policy question.

⁸⁶ A policy could be successful for these purposes if it is implemented effectively whether or not the policy is a good one.

