

THE OXFORD HANDBOOK OF

REGULATION

Edited by

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CHAPTER 7

ENFORCEMENT AND COMPLIANCE STRATEGIES

NEIL GUNNINGHAM

7.1 INTRODUCTION

Effective enforcement is vital to the successful implementation of social legislation, and legislation that is not enforced rarely fulfils its social objectives. This chapter examines the question of how the enforcement task might best be conducted in order to achieve policy outcomes that are effective (in terms of reducing the incidence of social harm) and efficient (in doing so at least cost to both duty holders and the regulator), while also maintaining community confidence.

It begins by examining the two strategies that for many years dominated the debate about enforcement strategy, the question of 'regulatory style' and whether it is more appropriate for regulators to 'punish or persuade'. Recognising the deficiencies of this dichotomy, it explores a number of more recent approaches that have proved increasingly influential on the policy debate. Such an examination must begin with John Braithwaite's seminal contribution and the arguments he makes in favour of 'responsive regulation'. This approach conceives of regulation in terms of dialogic regulatory culture in which regulators signal to industry their commitment to escalate their enforcement response whenever lower levels of intervention fail (Ayres and Braithwaite, 1992). Under this model, regulators begin by assuming virtue (to which they respond with cooperative measures) but when their expectations are

disappointed, they respond with progressively punitive/coercive strategies until the regulatee conforms.

This approach is taken further by Smart Regulation, which accepts Braithwaite's arguments as to the benefits of an escalating response up an enforcement pyramid but suggests that government should harness second and third parties (both commercial and non-commercial) as surrogate regulators, thereby achieving not only better policy outcomes at less cost but also freeing up scarce regulatory resources which can be redeployed in circumstances where no alternatives to direct government intervention are available. Further, whereas Braithwaite's pyramid utilises a single instrument category (state regulation) Smart Regulation argues that a range of instruments and parties should be invoked. Specifically, it makes the case for regulation and enforcement to be designed using a number of different instruments implemented by a number of parties, and it conceives of escalation to higher levels of coerciveness not only within a single instrument category but also across several different instruments and across different faces of the pyramid.

7.2 TO PUNISH OR PERSUADE?

Regulatory agencies have considerable administrative discretion with the enforcement task. In broad terms, they can choose between (or incorporate some mixture of) two very different enforcement styles or strategies: those of deterrence and 'advise and persuade' (sometimes referred to as a 'compliance' strategy).

The deterrence strategy emphasises a confrontational style of enforcement and the sanctioning of rule-breaking behaviour. It assumes that those regulated are rational actors capable of responding to incentives, and that if offenders are detected with sufficient frequency and punished with sufficient severity, then they, and other potential violators, will be deterred from violations in the future. The deterrence strategy is accusatory and adversarial. Energy is devoted to detecting violations, establishing guilt, and penalising violators for past wrongdoing.

In contrast, an 'advise and persuade' or 'compliance' strategy emphasises cooperation rather than confrontation and conciliation rather than coercion (Hutter, 1993). As described by Hawkins (1984: 4):

A compliance strategy seeks to prevent harm rather than punish an evil. Its conception of enforcement centres upon the attainment of the broad aims of legislation, rather than sanctioning its breach. Recourse to the legal process here is rare, a matter of last resort, since compliance strategy is concerned with repair and results, not retribution. And for compliance to be effected, some positive accomplishment is often required, rather than simply refraining from an act.

Bargaining and negotiation characterise a compliance strategy. The threat of enforcement remains, so far as possible, in the background. It is there to be employed mainly as a tactic, as a bluff, only to be actually invoked where all else fails; in extreme cases where the regulated entity remains uncooperative and intransigent.

These two enforcement strategies are two polar extremes, hypothetical constructs unlikely to be found in their pure form. Which of these enforcement strategies will achieve best results (or, if both fall substantially short, what alternative strategy should be preferred), can only be answered through an evidence-based analysis of the international literature. Most of that literature focuses on one end of the enforcement continuum and asks: how effective is deterrence in achieving improved regulatory outcomes? A more modest literature examines the opposite pole of the continuum and documents the considerable flaws in a pure 'advise and persuade' compliance strategy. Both of these bodies of literature are analysed below.

7.2.1 Assessing deterrence

Proponents of deterrence assume that regulated business corporations are 'amoral calculators' (Kagan and Scholz, 1984) that will take costly measures to meet public policy goals only when: (1) specifically required to do so by law and (2) they believe that legal non-compliance is likely to be detected and harshly penalised (Becker, 1968; Stigler, 1971). On this view, the certainty and severity of penalties must be such that it is not economically rational to defy the law. A distinction is made between general deterrence (premised on the notion that punishment of one enterprise will discourage others from engaging in similar proscribed conduct) and specific deterrence (premised on the notion that an enterprise that has experienced previous legal sanctions will be more inclined to make efforts to avoid future penalties). Both forms of deterrence are assumed to make a substantial positive contribution to reducing the social harm proscribed by regulation (Simpson, 2002).

But does the evidence support the 'common sense' view about the need for deterrence and, if so, in what circumstances? Is deterrence likely to have the same impact 'across the board' or might this vary between, for example, large corporations and small and medium sized enterprises, or between 'best practice' organisations and the recalcitrant? International evidence-based research indicates that the link between deterrence and compliance is complex.

In terms of general deterrence, the evidence shows that regulated business firms' *perceptions* of legal risk (primarily of prosecution) play a far more important role in shaping firm behaviour than the objective likelihood of legal sanctions (Simpson, 2002: ch. 2). And even when perceptions of legal risk are high, this is not necessarily an important motivator of behaviour. For example, Braithwaite and Makkai (1991: 35) found that in the case of nursing home regulation, there was virtually no correlation between facilities' regulatory compliance rates and their perceptions of the certainty

and severity of punishment for violations, except for certain minorities of actors in some contexts. Yet other well constructed studies have found that 'deterrence, for all its faults, may impact more extensively on risk management and compliance activity' than applying remedial strategies after the event (Baldwin, 2004: 373).

Haines (1997), in another important study, suggests that deterrence, while important in influencing the behaviour of small and medium sized enterprises, may have a much smaller impact on large ones. The simpler management structures of small firms and the relative incapacity of key decision-makers within them to avoid personal liability, also make them much easier targets for prosecution. The size of the penalty may also be an important consideration: mega-penalties tend to penetrate corporate consciousness in a way that other penalties do not (Gunningham, Kagan, and Thornton, 2005).

It is plausible however, that the deterrent impact of tough enforcement may be weaker today, than it was in past decades, at least in industries that have been subject to substantial regulation for a considerable period and/or are reputation sensitive. Significantly, Gunningham, Kagan, and Thornton's research (2005) on the heavily regulated electroplating industry and the brand-sensitive chemical industry found that the former believed (as a result of many years of targeted enforcement) that resistance to regulation was futile and they had little alternative but to comply, while the latter complied largely in order to protect their 'social licence to operate' rather than because of fear of prosecution. And, in both industries, almost half of respondents gave normative rather than instrumental explanations for why they complied. Many thought of themselves as 'good guys', complying with regulation because it was the right thing to do.

Nevertheless, they struggled to disentangle normative from instrumental motivations, and wrestled with the temptation to backslide when legally mandated improvements proved very expensive. Many acknowledged that, in the absence of regulation, it is questionable whether their firms' current good intentions would continue indefinitely—not only because their own motivation might decline but because they resented others 'getting away with it'. Strikingly, Gunningham, Kagan, and Thornton (2005) found that hearing about legal sanctions against other firms prompts many of them to review, and often to take further action to strengthen, their own firm's compliance programme.

From this it appears that in mature, heavily regulated industries such as mining, although deterrence becomes less important as a direct motivator of compliance, it nevertheless plays other important roles. In particular, for most respondents, hearing about sanctions against other firms had both a 'reminder' and a 'reassurance' function—reminding them to review their own compliance status and reassuring them that if they invested in compliance efforts, their competitors who cheated would probably not get away with it (Gunningham, Kagan, and Thornton, 2005). Thus general deterrence, albeit entangled with normative and other motivations, continued to play a significant role.

Turning to specific deterrence, the evidence of a link between past penalty and improved future performance is stronger, and suggests that a legal penalty against a company in the past influences their future level of compliance (Simpson, 2002). Baldwin and Anderson (2002: 10), for example, found that 71 per cent of companies that had experienced a punitive sanction reported that 'such sanctioning had impacted very strongly on their approach to regulatory risks... For many companies the imposition of a first sanction produced a sea change in attitudes.' However, the literature also suggests that action falling short of prosecution (for example, inspection, followed by the issue of administrative notices or administrative penalties) can also achieve 'a re-shuffling of managerial priorities' (Baggs, Silverstein, and Foley, 2003: 491) even when those penalties are insufficient as to justify action in pure cost-benefit terms (Gray and Scholz, 1993). This seems to be because such action is effective in refocusing employer attention on social problems they may previously have ignored or overlooked. But routine inspections without any form of enforcement apparently have no beneficial impact (Shapiro and Rabinowitz, 1997: 713).

Against the positive contribution that deterrence can make in *some* circumstances, must be weighed the counter-productive consequences of its over-use or indiscriminate use. For: 'if the government punishes companies in circumstances where managers believe that there has been good faith compliance, corporate officers may react by being less cooperative with regulatory agencies' (Shapiro and Rabinowitz, 1997: 718). Indeed, there is evidence that managers may refuse to do anything more than minimally comply with existing regulations (rather than seeking to go beyond compliance) and frequently resist agency enforcement efforts. In some cases, Bardach and Kagan (1982) demonstrate that the result is a 'culture of regulatory resistance' amongst employers.

For the purposes of this chapter, perhaps the most important conclusion may be that those who are differently motivated are likely to respond very differently to a deterrence strategy. While it may be effective when applied to the recalcitrant and perhaps to reluctant compliers it will be counter-productive as regards corporate leaders who respond badly to an adversarial approach (Bardach and Kagan, 1982) and irrelevant to the incompetent. But inspectors are, for the most part, incapable of knowing the motivation of those they are regulating, with the result that a 'pure' deterrence strategy may achieve very mixed results.

The broader message may be that the impact of deterrence is significant but uneven and that unless it is used wisely and well, it may have negative consequences as well as positive ones. How to steer a middle path that harnesses the positive impact of deterrence, and targets it to those whose behaviour is most likely to be impacted by it, while minimising its adverse side effects, are issues which will be further explored later in this chapter.

7.2.2 Assessing compliance

Although the above section has cautioned against over-reliance on deterrence, there are also dangers in adopting a pure 'advise and persuade'/compliance oriented strategy of

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enforcement, which can easily degenerate into intolerable laxity and fail to deter those who have no interest in complying voluntarily (Gunningham, 1987). More broadly, there is considerable evidence that cooperative approaches may actually *discourage* improved regulatory performance amongst better actors if agencies permit lawbreakers to go unpunished. This is because even those who are predisposed to be 'good apples' may feel at a competitive disadvantage if they invest money in compliance at a time when others are seen to be 'getting away with it' (Shapiro and Rabinowitz, 1997).

The counter-productive effects of a pure compliance strategy are illustrated by Gunningham's (1987) study of the New South Wales Mines Inspectorate in its approach to the inspection and enforcement of legislation relating to the safe use of asbestos. The study documented how the inspectorate was not only loath to prosecute, even when faced with evidence of gross breaches of the asbestos regulations, but routinely warned mine management of prospective inspections, thereby enabling them to clean up and disguise many of the worst regulatory breaches. That analysis (Gunningham, 1987: 91) concluded that:

What the Mines Inspectorate provided at Baryulgil... fell far short of any... optimum. Its approach might best be classified as 'negotiated non-compliance', a strategy located at the compliance extreme of the compliance-deterrence continuum, a complete withdrawal from enforcement activity, a toothless, passive and acquiescent approach which, however attractive to the regulatory agency and to the regulated industry, has tragic consequences for those whom the legislation is ostensibly intended to protect.

Again, the broader point is that a compliance strategy will have a different impact on differently motivated organisations. It may be entirely appropriate for corporate leaders but, as the Baryulgil example demonstrates, it will manifestly not be effective in engaging with reluctant compliers or the recalcitrant, and only effective for the incompetent if it is coupled with education and advice. Once again, regulators who are unable to determine the sort of organisation they are dealing with will be operating largely in the dark and unable to use this strategy in the most constructive fashion.

7.3 RESPONSIVE REGULATION

Unsurprisingly, given the limitations of both compliance and deterrence as 'stand alone' strategies, most contemporary regulatory specialists now argue, on the basis of considerable evidence from both Europe and the USA, that a judicious *mix* of compliance and deterrence is likely to be the optimal regulatory strategy (Ayres and Braithwaite, 1992; Kagan, 1994; Wright, Marsden, and Antonelli, 2004). But how might such a mix best be achieved and what would an ideal combination of cooperation and punishment look like?

Because regulated enterprises have a variety of motivations and capabilities, it is suggested that regulators must invoke enforcement strategies which successfully deter egregious offenders, while at the same time encouraging virtuous employers to comply voluntarily and rewarding those who are going 'beyond compliance'. Thus, good regulation means invoking different responsive enforcement strategies depending upon whether one is dealing with leaders, reluctant compliers, the recalcitrant, or the incompetent. However, the dilemma for regulators is that it is rarely possible to be confident in advance as to the motivation of a regulated firm.

If the regulator assumes all firms will behave as good corporate citizens, it may devise a regulatory strategy that stimulates voluntary action but which is incapable of effectively deterring those who have no interest in responding to encouragement to voluntary initiatives. On the other hand, if regulators assume all firms face a conflict between safety and profit, or for other reasons that they will require threatening with a big stick in order to bring them into compliance, then they will unnecessarily alienate (and impose unnecessary costs on) those who would willingly comply voluntarily, thereby generating a culture of resistance to regulation (Bardach and Kagan, 1982).

The challenge is to develop enforcement strategies that punish the worst offenders, while at the same time encouraging and helping employers to comply voluntarily. The most widely applied mechanism for resolving this challenge is that proposed by Ayres and Braithwaite, namely for regulators to apply an 'enforcement pyramid' (see Figure 7.1 below) which employs advisory and persuasive measures at the bottom, mild administrative sanctions in the middle, and punitive sanctions at the top. On their view, regulators should start at the bottom of the pyramid assuming virtue—that business is willing to comply voluntarily. However, where this assumption is shown to be ill-founded regulators should escalate up the enforcement pyramid to increasingly deterrence-orientated strategies (see Ayres and Braithwaite, 1992; Gunningham and Johnstone, 1999). In this manner they find out, through repeat interaction, whether they are dealing with leaders, reluctant compliers, the recalcitrant, or the incompetent, and respond accordingly.

Central to this model are the need for (i) gradual escalation up the face of the pyramid and (ii) the existence of a credible peak or tip which, if activated, will be sufficiently powerful to deter even the most egregious offender. The former (rather than any abrupt shift from low to high interventionism) is desirable because it facilitates the 'tit-for-tat' response on the part of regulators which forms the basis for responsive regulation (i.e. if the duty holder responds as a 'good citizen' they will continue to be treated by the inspectorate as a good citizen—Ayres and Braithwaite, 1992). The latter is important not only because of its deterrent value, but also because it ensures a level playing field in that the virtuous are not disadvantaged.

Six broader points must be made about the enforcement pyramid.

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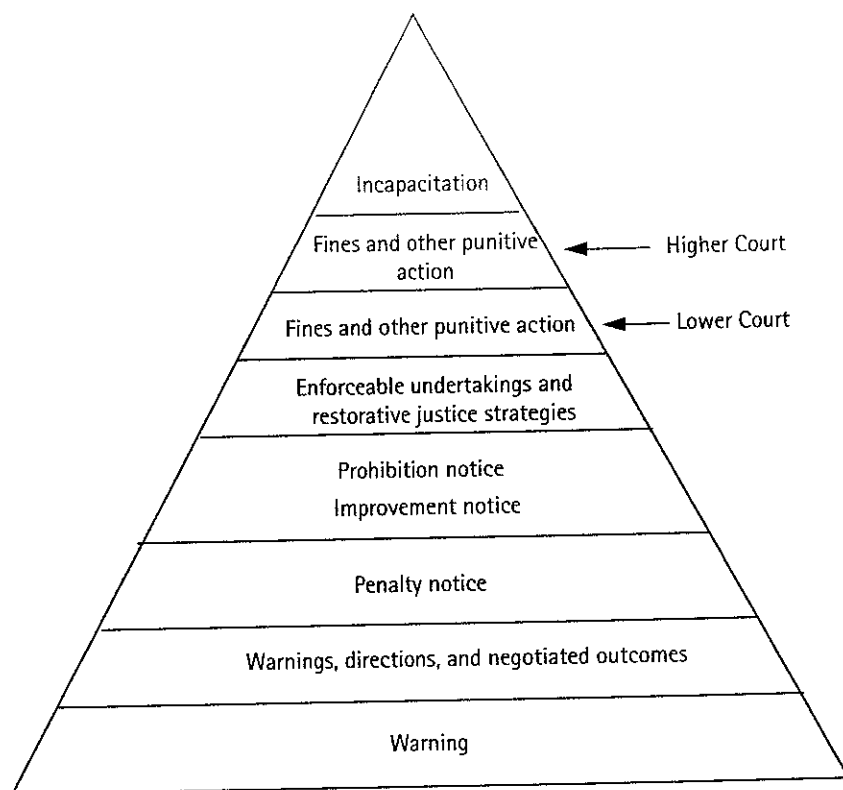


Figure 7.1 Enforcement Pyramid

The enforcement pyramid set out above is illustrative of the sorts of carrots and sticks that an agency might wish to invoke as part of an escalating strategy of enforcement but it is not intended to be exclusionary. Many different mechanisms might be utilised under this general approach.

- (1) Haines has suggested that 'escalating and de-escalating of penalty may be far more complex than the proponents of pyramidal enforcement contemplate' (Haines, 1997: 219–20). Not least, regulators who escalate sanctions may produce unintended consequences in companies, 'which in response to threat, aim to reduce their vulnerability to scrutiny, and so, to liability . . . When escalation of penalty occurs, motivation for corporate compliance shifts from co-operation and trust, to deterrence and mistrust' (Haines, 1997: 119). In this way, chronically mistrustful organisations may be created. As she points out: building trust with organisations who have never experienced legal threat may be one thing, rebuilding trust may be an entirely different matter' (Haines, 1997: 120).
- (2) As Christine Parker (1999: 223) has argued:

strategic compliance-oriented enforcement strategies do not ensure that regulators' messages of encouragement of compliance reach an audience equipped to understand or effectively respond to them. The application of the pyramid must eventually lead to

the creation of a pool of compliance expertise in the corporate world, otherwise efforts to respond to regulatory messages will be ineffectual.

In essence, a pyramidal response will not be enough unless information flows effectively from regulator to regulated and there is a capacity for a genuine dialogue to take place. If for example, the regulator sends a signal at a low point in the enforcement pyramid to senior management who, preoccupied with production and other pressures, fail to appreciate its significance or respond with tokenism, or creative compliance then little will have been achieved. Certainly it is important to engage with senior management—without their 'buy in' no substantive improvement in regulatory performance may be possible. But such engagement may only prove practicable through a trusted intermediary such as a compliance professional, capable of harmonising regulatory goals and organisational norms. Parker argues that, for this reason, it may be particularly important to nurture compliance professionalism (for example, through associations of safety professionals) in order both to create allies in the enterprise and a community with which regulators can communicate. Sometimes they alone have both an understanding of the key regulatory issues, and a capacity to put the 'business case' for resolving them, in credible terms, to senior corporate management (see also Rees, 1988).

- (3) In circumstances where the classification of regulated enterprises into one of a variety of motivational postures (e.g. Occupational Health and Safety (OHS) leaders, reluctant compliers, incompetents, and the recalcitrant) is relatively straightforward, then a target-analytic approach might be preferred to a responsive tit-for-tat strategy (Kagan and Scholz, 1984). For example, if experience suggested that the very large majority of a sub-group of regulated enterprises was rationally recalcitrant then the bottom half of the pyramid response might be dispensed with in favour of deterrence. Indeed, Braithwaite's version of responsive regulation has shifted over the years to the extent that he now takes account of the possibility that different motivational postures might lend themselves to different strategies (2002: 36–40; see also V. Braithwaite, 2008). Nevertheless, negotiation would still remain at the heart of his approach, which seeks to integrate target-analytic with responsive enforcement strategies rather than to choose between them.
- (4) A recent and increasingly influential approach is that of 'risk-based' regulation, which argues that regulatory agencies should rely primarily on targeting their inspection and enforcement resources based on an assessment of the degree of risk posed by a regulated entity (Black, 2005; Hampton, 2005) rather than relying upon gradual escalation up an enforcement pyramid. Nevertheless, a number of serious challenges confront risk-based regulation, including the danger of focusing on a small number of large risks to the exclusion or under-enforcement of a large number of low risks (Black, 2005 and 2006). Whether the result will be an overall reduction in the level of risk may depend substantially

- on the context and degree of sophistication of the risk analysis and quality of evidence available. In any event, risk based regulation and the enforcement pyramid are not necessarily antithetical since a pyramidal response might be applied to enterprises that had first been targeted on the basis of a risk assessment.
- (5) Baldwin and Black (2008: 45) have further emphasised the difficulties of a pyramidal approach and responsive regulation generally, 'in polycentric regulatory regimes, including those where the roles of policymaking, information gathering and enforcement are distributed between a number of organisations, particularly where they cross different jurisdictional boundaries'. Since in modern complex societies, polycentric regulatory regimes are the norm rather than the exception, this critique, if substantiated, has important practical implications.
 - (6) Finally, in many industries there are insufficient repeat interactions between regulator and regulated as to make a pyramidal approach viable in practice (Gunningham and Johnstone, 1999: 123-9). Moreover, as Richard Johnstone (2003: 18) has argued:

for the pyramid to work in the interactive, 'tit for tat' sense envisaged by its proponents, the regulator needs to be able to identify the kind of firm it is dealing with, and the firm needs to know how to interpret the regulators' use of regulatory tools, and how to respond to them (Black, 2001: 20). This requires regulators not only to know what is entailed in effective compliance programs and systematic OHSM approaches, but also to have a sophisticated understanding of the contexts within which organisations operate, and the nature of an organisation's responses to the various enforcement measures.

All this, as Johnstone points out, is a tall order. The result is likely to be that the less intense and the less frequent is the level of inspection, and the less knowledge the regulator is able to glean as to the circumstances and motivations of regulated firms, the less practicable it becomes to apply a pyramidal enforcement strategy.

Although the first five concerns are often capable of being addressed, the sixth often is not. Indeed, if repeat interactions are not possible then some commentators have concluded that the entire enforcement pyramid has little practical application (Scott, 2004). While this might arguably be correct in particular circumstances, it is manifestly incorrect for industries that have traditionally been subject to a high degree of regulation. For example, with regard to OHS in hazardous industries like mining, large companies at least, can expect a substantial number of inspections each year and a level of regulatory scrutiny that enables inspectors to gain considerable knowledge about their behaviour and motivations.

For these firms in particular, a tit-for-tat strategy is entirely credible and the enforcement pyramid can provide a key conceptual underpinning to an effective range of inspection and enforcement tools. For such enterprises, it encapsulates the virtues of responsive regulation: regulation that takes account of, and responds to, the

regulatory capacities that already exist within regulated firms. In doing so, it offers a strategy whereby regulators can successfully deter egregious offenders, while at the same time encouraging and helping the majority of employers to comply voluntarily.

But where regulators make only occasional visits (as may be the case with small companies), and where the reach of the state is seriously constrained, then the pyramid has more limited application. Here, many capable and experienced regulators ask: 'given all the circumstances, which enforcement technique is most likely to result in a lasting improvement . . . , while retaining the confidence of stakeholders' (Kruse and Wilkinson, 2005: 5). Such regulators would conceive of their choices not in terms of a pyramid, but rather in terms of a segmented circle, from which they will simply choose the most appropriate regulatory tool from a variety of options. That is, the regulator's best option may be to simply make a judgment as to a company or individual's willingness and capacity to comply with the rules, and match their enforcement style with the image of their targets (Hawkins, 1984; Westrum, 1996). In doing so, they usually reserve coercive sanctions for a small minority of perceived 'bad apples' (Makkai and Braithwaite, 1994).

But even where regulators find it impractical to use the pyramid in its entirety, it may nevertheless be useful in determining which regulatory tool to employ in a given instance—that is, at what point in the pyramid would it be appropriate to intervene, given the characteristics of the regulated entity and the degree of risk or type of breach (Gunningham and Johnstone, 1999: 124–5). This involves a hybrid approach—somewhere between the dynamic and ongoing nature of a full 'tit-for-tat' responsive regulatory strategy and the sort of static proportional response contemplated, for example, by the UK Health and Safety Executive's enforcement management model (HSE, 2002). In particular, it involves gleanings as much information as possible from the previous history and track record of the duty holder, from such indicators as are available and their managers' attitudes, as to inform an at least partially responsive approach as to where in the enforcement pyramid to intervene.

Finally, the pyramidal approach: 'has the great merit that when shown the various pyramids, many regulators and policy-makers immediately seem to understand them descriptively and offer examples' (Scott, 2004: 160). That is, connecting the theoretical construct of the pyramid to the concrete and practical experience of regulators is not a substantial problem, although their conception of it is usually more static than responsive.

Of course, regulation sometimes plays out differently in different national or socio-economic settings. For example, regulation in the United States is strongly shaped by a cultural mistrust of government and business, and a concern to avoid regulatory capture. The result, as Robert Kagan (2003) has so eloquently shown, is a process of 'adversarial legalism' by which policy making and implementation are dominated by lawyers and litigation and regulators are predisposed to imposed legal penalties on

wrongdoers. In comparison, regulation in other economically advanced countries tends to be much more conciliatory, with penalties often being invoked only as a last resort. Responsive regulation, however, would claim to be equally comfortable in addressing either of these approaches to regulation, castigating the first for going directly to the top of the pyramid without taking advantage of the opportunities for better outcomes at lower levels and the latter for an unwillingness to escalate up the pyramid when advice and persuasion fail to work.

7.4 SMART REGULATION

Gunningham and Grabosky (1999) advocate the concept of 'Smart Regulation', a term they use to refer to an emerging form of regulatory pluralism that embraces flexible, imaginative, and innovative forms of social control which seek to harness not just governments but also business and third parties. For example, it is concerned with self-regulation and co-regulation, with using both commercial interests and NGOs (non-governmental organisations) and with finding surrogates for direct government regulation, as well as with improving the effectiveness and efficiency of more conventional forms of direct government regulation.

The central argument is that, in the majority of circumstances, the use of multiple rather than single policy instruments and a broader range of regulatory actors, will produce better regulation. Further, that this will allow the implementation of complementary combinations of instruments and participants tailored to meet the imperatives of specific environmental issues. It is however, as Scott (2004) points out, an approach that privileges state law rather than treats the state as simply one of a number of governance institutions.

To put Smart Regulation in context, it is important to remember that traditionally, regulation was thought of as a bi-partite process involving government and business, with the former acting in the role of regulator and the latter as regulatee. However, a substantial body of empirical research reveals that there is a plurality of regulatory forms, that numerous actors influence the behaviour of regulated groups in a variety of complex and subtle ways (Rees, 1988: 7), and that mechanisms of informal social control often prove more important than formal ones. Accordingly, the Smart Regulation perspective suggests that we should focus our attention on such broader regulatory influences as: international standards organisations; trading partners and the supply chain; commercial institutions and financial markets; peer pressure and self-regulation through industry associations; internal environmental management systems and culture; and civil society in a myriad of different forms.

In terms of its intellectual history, Smart Regulation evolved in a period in which it had become apparent that neither traditional command and control regulation nor the free market provides satisfactory answers to the increasingly complex and serious environmental problems which confront the world. It was this that led to a search for alternatives more capable of addressing the environmental challenge, and in particular to the exploration of a broader range of policy tools such as economic instruments,¹ self-regulation, and information-based strategies. Smart Regulation also emerged in a period of comparative state weakness, in which the dominance of neoliberalism had resulted in the emasculation of formerly powerful environmental regulators and in which third parties such as NGOs and business were increasingly filling the 'regulatory space' formerly occupied by the state.

In terms of enforcement, Smart Regulation builds on John Braithwaite's 'enforcement pyramid', and argues that it is possible to reconceptualise and extend the enforcement pyramid in two important ways.

- (1) Beyond the enforcement roles of the state, it is possible for both second and third parties to act as quasi-regulators. In this expanded model, escalation would be possible up any face of the pyramid, including the second face (through self-regulation), or the third face (through a variety of actions by commercial or non-commercial third parties or both), in addition to government action. To give a concrete example of escalation up the third face, the developing Forest Stewardship Council (FSC) is a global environmental standards setting system for forest products. The FSC will both establish standards that can be used to certify forestry products as sustainably managed and will 'certify the certifiers'. Once operational, it will rely for its 'clout' on changing consumer demand and upon creating strong 'buyers groups' and other mechanisms for institutionalising green consumer demand. That is, its success will depend very largely on influencing consumer demand. While government involvement, for example through formal endorsement or through government procurement policies which supported the FSC, would be valuable, the scheme is essentially a free standing one: from base to peak (consumer sanctions and boycotts) the scheme is entirely third party based. In this way, a new institutional system for global environmental standard-setting will come about, entirely independent of government. (see Meidinger, 1996).
- (2) Braithwaite's pyramid utilises a single instrument category, specifically, state regulation, rather than a range of instruments *and parties*. In contrast, the Smart Regulation pyramid conceives of the possibility of regulation using a number of different instruments implemented by a number of parties. It also conceives of escalation to higher levels of coerciveness not only within a single instrument category but also across several different instruments and across different faces of the pyramid. A graphic illustration of exactly how this can indeed occur is provided by Joe Rees's analysis of the highly sophisticated

self-regulatory programme of the Institute of Nuclear Power Operators (INPO), which, post Three Mile Island, is probably amongst the most impressive and effective of such schemes worldwide (see Rees, 1994). However, even INPO is incapable of working effectively in isolation. There are, inevitably, industry laggards, who do not respond to education, persuasion, peer group pressure, gradual nagging from INPO, shaming, or other instruments at its disposal. INPO's ultimate response, after five years of frustration, was to turn to the government regulator, the Nuclear Regulatory Commission (NRC). That is, the effective functioning of the lower levels of the pyramid may depend upon invoking the peak, which in this case, only government could do. As Rees puts it (1994: 117): 'INPO's climb to power has been accomplished on the shoulders of the NRC.'

This case also shows the importance of integration between the different levels of the pyramid. The NRC did not just happen to stumble across, or threaten action against recalcitrants. Rather, there was considerable communication between INPO and the NRC which facilitated what was, in effect, a tiered response of education and information, escalating through peer group pressure and a series of increasingly threatening letters, ultimately to the threat of criminal penalties and incapacitation. Criminal penalties were sanctions that government alone could impose, but the less interventionist strategies lower down the pyramid were approaches which, in these circumstances at least, INPO itself was in the best position to pursue. Thus, even in the case of one of the most successful schemes of self regulation ever documented, it was the presence of the regulatory gorilla in the closet that secured its ultimate success.

It is not intended to give the impression, however, that a coordinated escalation up one or more sides of our instrument pyramid is practicable in all cases. On the contrary, controlled escalation is only possible where the instruments in question lend themselves to a graduated, responsive, and interactive enforcement strategy. The two instruments which are most amenable to such a strategy (because they are readily manipulated) are command and control and self-regulation. Thus, it is no coincidence that the first example of how to shift from one face of the pyramid to another as one escalates and of how to invoke the dynamic peak was taken from precisely this instrument combination. However, there are other instruments which are at least partially amenable to such a response, the most obvious being insurance and banking.

A combination of government mandated information (a modestly interventionist strategy) in conjunction with third party pressure (at the higher levels of the pyramid) might also be a viable option. For example, government might require business to disclose various information about its level of emissions under a Toxic Release Inventory, (see Gunningham and Cornwall, 1994), leaving it to financial markets, insurers (commercial third parties), and environmental groups (non-commercial third parties) to use that information in a variety of ways to bring pressure on poor environmental performers (see Hamilton, 1995).

In contrast, in the case of certain other instruments, the capacity for responsive regulation is lacking, either because an individual instrument is not designed to facilitate responsive regulation (i.e. its implementation is static rather than dynamic and cannot be tailored to escalate or de-escalate depending on the behaviour of specific firms) or because there is no potential for coordinated interaction between instruments. Another limitation is the possibility that in some circumstances, escalation may only be possible to the middle levels of the pyramid, with no alternative instrument or party having the capacity to deliver higher levels of coerciveness. Or a particular instrument or instrument combination may facilitate action at the bottom of the pyramid and at the top, but not in the middle levels, with the result that there is no capacity for gradual escalation. In the substantial range of circumstances when coordinated escalation is not readily achievable, a critical role of government will be, so far as possible, to fill the gaps between the different levels of the pyramid, seeking to compensate for either the absence of suitable second or third party instruments, or for their static or limited nature, either through direct intervention or, preferably, by facilitating action or acting as a catalyst for effective second or third party action. In effect, a major role for government is thus to facilitate second and third parties climbing the pyramid.

Finally, Smart Regulation cautions that there are two general circumstances where it is inappropriate to adopt an escalating response up the instrument or enforcement pyramid, irrespective of whether it is possible to achieve such a response. First, in situations which involve a serious risk of irreversible loss or catastrophic damage, then a graduated response is inappropriate because the risks are too high: the endangered species may have become extinct, or the nuclear plant may have exploded, before the regulator has determined how high up the pyramid it is necessary to escalate in order to change the behaviour of the target group. In these circumstances a horizontal rather than a vertical approach may be preferable: imposing a range of instruments, including the underpinning of a regulatory safety net, simultaneously rather than sequentially (see Gunningham and Young, 1997). Second, a graduated response is only appropriate where the parties have continuing interactions—it is these which makes it credible to begin with a low interventionist response and to escalate (in a tit-for-tat response) if this proves insufficient. In contrast, where there is only one chance to influence the behaviour in question (for example because small employers can only very rarely be inspected), then a more interventionist first response may be justified, particularly if the risk involved is a high one.

In summary, the preferred role for government under Smart Regulation is to create the necessary preconditions for second or third parties to assume a greater share of the regulatory burden rather than engaging in direct intervention. This will also reduce the drain on scarce regulatory resources and provide greater ownership of regulatory issues by industry and the wider community. In this way, government acts principally as a catalyst or facilitator. In particular, it can play a crucial role in enabling a coordinated and gradual escalation up an

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instrument pyramid, filling any gaps that may exist in that pyramid and facilitating links between its different layers.

7.5 META-REGULATION

In recent years it has been recognised that there is another enforcement model which, like smart regulation, also seeks to identify a 'surrogate regulator' and to minimise the hands-on enforcement role of the state. This strategy, known as 'meta-regulation' or 'meta risk management', involves government, rather than regulating directly, risk-managing the risk management of individual enterprises.

Under such an approach, the role of regulation ceases to be primarily about government inspectors checking compliance with rules, and becomes more about encouraging the industry to put in place its own systems of internal control and management which are then scrutinised by regulators. Rather than regulating prescriptively, meta-regulation seeks by law to stimulate modes of self-organisation within the firm in such a way as to encourage internal self-critical reflection about its regulatory performance. In so doing, it 'forces companies to evaluate and report on their own self-regulation strategies so that regulatory agencies can determine [that] the ultimate objectives of regulation are being met'. As such, it provides 'self-regulation standards against which law can judge responsibility, companies can report and stakeholders can debate' (Parker, 2002: 246).

Under meta-regulation, the primary role of the inspectorate becomes that of 'regulating at a distance', relying upon the organisation itself to put in place appropriate systems and oversight mechanisms, but taking the necessary action to ensure that these mechanisms are working effectively. But as Hopkins and Wilkinson (2005: 9) have emphasised, the regulator's job under this approach is far more than passive compliance monitoring or the oversight of mere 'paper systems'. Rather it involves actively challenging the enterprise to demonstrate that its systems work in practice, scrutinising its risk management measures, and judging if the company 'has the leadership, staff, systems and procedures' to meet its regulatory obligations.

Some writers now see meta-regulation as an attractive alternative to a prescriptive standards (which tell duty holders precisely what measures to take²) or even to a performance-based rules regime (which specify outcomes or the desired level of performance—see Bluff and Gunningham, 2004). They recognise that the capacity to deal with complex organisations and complex regulatory problems through rules alone is limited and argue that it would be better to design a form of responsive regulation that induces companies themselves to acquire the specialised skills and knowledge to self-regulate,

subject to state and third party scrutiny. Indeed, some suggest that the only viable means of achieving social goals such as OHS is for organisations and companies, who know their own operations and facilities better than anyone, to take on the regulatory tasks themselves subject to government oversight. In this vein, writers variously talk about the need to engage with 'organisational or management failure' (Mitchison, 1999: 32) rather than merely with technical measures, and to encourage and facilitate greater 'reflexivity' on the part of the organisation as a whole (Teubner, 1983: 239; Teubner, Farmer, and Murphy, 1994) and to encourage companies not only to design their own self-regulatory processes but also 'to engage in self-evaluation of those processes as an integral part of their broader regulatory requirements' (Parker, 2002: 283).

To illustrate this general approach, take perhaps the longest standing and most sophisticated meta-regulatory regime in existence, the 'safety case'. This was first instituted on North Sea oil rigs following the Cullen enquiry into the Piper Alpha disaster (Cullen, 1990) and was subsequently adopted in the European Union with regard to Major Hazard Facilities (MHF) under the Seveso II Directive. Under this approach, responsibility is placed on the operator of a MHF to submit their plans for ensuring the safety of the facility to the regulator (or conceivably a third party) for approval. Those plans are then audited and, if satisfactory, form the basis for accreditation. The regulator's role is not to prescribe what action should be taken by the operator but to accredit the Safety Case and oversee its implementation. Although there is no single 'safety case' model (for example, see Nicol, 2001; Pitblado and Smith, 2001; Rasche, 2001; Wilkinson, 2002), this general approach usually includes an obligation for the operator to develop a comprehensive and systematic risk analysis in conjunction with controls and a safety management system which addresses the findings of that analysis. Conventionally, this is achieved by requiring the organisation seeking accreditation to make a 'safety case' to the regulator, by submitting documentary evidence that: (i) The safety management system is adequate to ensure compliance with statutory requirements and for the management of all aspects of the adopted major risk control measures; (ii) Adequate arrangements have been made for audit for the safety management system, and for audit reporting; (iii) All hazards with the potential to cause a major accident have been identified, the risk systematically evaluated and measures taken to reduce the risk to people affected by those hazards to as low as reasonably practicable (MISHC, 2001); and (iv) There is adequate involvement of key stakeholders (employees and contractors, other operators/suppliers, emergency services and so forth).

Crucial to the success both of the system and the safety case, will be the development of appropriate performance measures, for it is these which determine whether safety plans have been implemented and key objectives achieved (significantly, the Cullen Report referred to the centrality of a 'goal-setting' regime). Provided such measures are in place then it should be possible for either the inspectorate (or a third party auditor) to audit the system and the safety case

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effectively. In effect, the agency (or third party) will say, 'you draw up a plan and we will inspect you against it'. The performance and other indicators that will allow this to be done should be determined during the initial baseline audit in the course of which the enterprise and the agency/or third party auditor agree on both performance indicators and benchmarks, and the latter satisfies itself of their adequacy for their purpose. The outcome should be an agreed plan of how the enterprise intends to proceed and how to measure progress against the baseline. The safety case is sometimes described as 'the new prescription' (Hopkins, 2000: 99) because although what the operator must do is not prescribed, the processes they must go through, are indeed set out in considerable detail.

However, a safety case regime is no panacea and any industry contemplating such a regime must overcome a number of substantial challenges. A safety case regime relies heavily on 'process based' approaches such as management systems and risk-management more generally. Notwithstanding the attractions of such standards, they cannot be relied upon in isolation to bring about improved regulatory performance. The existence of a formal safety system or plan tells one very little about whether or to what extent production targets took precedence over safety, whether production pressures led to risk taking, or whether staffing levels at a given facility were inadequate and, if so, whether this had an adverse impact on safety. The formal system does not reveal to what extent near misses and incidents are actually reported (no matter how comprehensive the reporting system is in principle), or to what extent or why, workers are constrained from reporting their concerns. And, depending on the auditing process, it may not reveal how often safety meetings actually took place or if they did, whether they engaged with serious safety issues or were tokenistic in nature, or whether worker representatives were constrained from bringing certain safety issues before them. Audits of a safety management system or plan can also have serious limitations.

All of the above suggests that systems, plans, and processes have the potential to fail, both in their design and in their implementation. However, such a failure is far from inevitable. On the contrary, there is qualified evidence that carefully designed, systems-based approaches such as safety case, coupled with management commitment and the resources to make them work, can deliver substantial and sustained improvements in performance (Bluff, 2003). For example, Coglianese and Lazar (2003: 724) conclude from a broad survey that, 'management based' regulatory strategies such as management systems, do have a positive effect but 'not always unambiguously so', while a major United States study also found that generally, environmental management systems had positive effects on facilities' environmental performance (National Database on EMS, 2003). However, the evidence is not all in one direction, with one substantial European study finding that there is currently no evidence to suggest that environmental management systems have a *consistent* and *significant* positive impact on environmental performance (Tyteca and Carlens, 2002). Subsequently, a 2006 Australian study (Parker and Nielsen, 2006a)

has found that compliance systems implementation in the trade practices context was partial, symbolic, and half-hearted.

There could be a variety of reasons for these mixed results, including the possibility that some companies adopted such systems (which in environmental protection are usually voluntary) for cosmetic reasons (such as to maintain public legitimacy—see, for example, Power, 2004) rather than to improve performance. If so, then the principal problem is not with the system itself, but with the motivations of those who adopt it. Indeed it may be that safety cases and management systems like other process based tools, are just that—tools—and that they can only be effective when implemented with genuine commitment on the part of management.

This is broadly the conclusion of a number of studies in a variety of closely related areas of social regulation. For example, Gunningham, Kagan, and Thornton (2003: ch. 5) found that management style and motivation are more important in shaping the environmental (and presumably the OHS) performance of firms, than the system itself. In essence, management matters far more than management systems. Other studies too, have found that even the most well designed systems will only be effective where those who design and implement them are sufficiently motivated to make them succeed (Vectra, 2003).

Put differently, it is the *quality* of action taken to manage OHS that makes a difference to OHS performance and not just particular procedures or systems. This is consistent with the finding of Parker and Nielsen that formal compliance system implementation can only contribute to better compliance through better compliance management *in practice*, which in turn is underpinned by the organisation's level of commitment to values that support compliance, organisational resources and managerial competence. As they put it: 'right managerial values may be more significant than right managerial activity' (Parker and Nielsen, 2006b: 12).

These findings raise issues which go to the heart of the question: to what extent can meta-regulation (via systems, plans, and risk management more generally) influence regulatory outcomes? Are policy makers mistaken in their belief that those who are required to jump over various hurdles (developing and implementing plans and systems, adopting a safety case) will as a result improve both their attitudes and performance?

Certainly, industry leaders may use plans and systems to improve regulatory outcomes (they are powerful tools in the hands of motivated management), but they would be doing much the same even in the absence of regulation. However, it is far from clear that reluctant compliers, the recalcitrant, or incompetent will behave similarly. Implementing a safety case or management systems and management plans is complex, expensive, and resource intensive. In the absence of management commitment—perhaps coupled with sufficient resources, and the necessary capacity and expertise (Bluff, 2003)—such systems may be more honoured in the breach and fall foul to many of the pitfalls identified above. If these

challenges cannot be overcome then mandating systematic risk analysis, controls, and a management system under a safety case regime may be more a regulatory blind alley, than a route to best practice.

Another concern with meta-regulation is that its focus on corporate responsibility processes may result in companies avoiding accountability for substance, if not for form. For example, Julia Black (2005: 544–5) points to the risks that:

the firm's internal controls will be directed at ensuring the firm achieves the objectives it sets for itself: namely profits and market share. Whilst proponents of meta-regulation are correct to argue that its strength lies in the ability to leverage off a firm's own systems of internal control, and indeed that regulators should fashion their own regulatory processes on those controls, this difference in objectives means that regulators can never rely on a firm's own systems without some modifications. The problem then arises, however, of locating those differences, and ensuring both regulator and regulated understand them.

Parker in contrast, suggests that it is possible, in principle at least, to imagine legal meta-regulation that holds business organisations accountable for putting in place corporate conscience processes that are aimed at substantive social values, albeit that this can only be achieved by ensuring that, 'procedural and substantive rights of customers, employees, local communities and other relevant stakeholders, as against businesses, are adequately recognised and protected' (Parker, 2007). Quite how wide is the gap between Parker's ideal and the actual practice of meta-regulation is an open question.

7.6 CONCLUSION

Neither compliance nor deterrence has proved effective or efficient enforcement strategies. The evidence suggests that a compliance strategy, while valuable in encouraging and facilitating those willing to comply with the law to do so, may prove disastrous against 'rational actors' who are not disposed to voluntary compliance. And while deterrence can play an important positive role, especially in reminding firms to review their compliance efforts and in reassuring them that if they comply, others will not be allowed to 'get away with it', its impact is very uneven. Deterrence is, for example, more effective against small organisations than large ones and better at influencing rational actors than the incompetent. Unless it is carefully targeted, it can actually prove counterproductive, as when it prompts firms and individuals to develop a 'culture of regulatory resistance' or to take a defensive stand, withholding information and failing to explore the underlying cause of a problem for fear that this information will be used against them in a court of law.

Responsive regulators have found that they will gain better results by developing more sophisticated strategies which employ a judicious blend of persuasion and coercion, the actual mix being adjusted to the particular circumstances and motivations of the entity with whom they are dealing. A valuable heuristic, in thinking about how best to tailor enforcement strategy to individual circumstances, is that of the enforcement pyramid. This embraces an approach which rewards virtue while punishing vice and in which the regulator is responsive to the past action of the regulated entity. Thus, although it is not possible for the regulator to be confident at the outset, of a duty holder's motivation, or whether they are an industry leader, a reluctant complier, a recalcitrant or incompetent, this will gradually become apparent through the tit-for-tat strategy of pyramidal enforcement.

The enforcement pyramid approach is best suited to the regulation of large organisations with which the regulator has frequent interactions. However, it can also be of use in determining which enforcement tool is most suited to the particular circumstances of a smaller enterprise with which they have infrequent contact. Here, its value is in providing guidance as to which arrow to select from the quiver, rather than to how best to conduct a series of repeat interactions.

Smart Regulation attempts to expand upon some of the insights of responsive regulation and the enforcement pyramid, by suggesting how public agencies may harness institutions and resources residing *outside* the public sector (in conjunction with a broader range of complementary policy instruments) to further policy objectives. In particular, it argues that markets, civil society, and other institutions can sometimes act as surrogate regulators and accomplish public policy goals more effectively, with greater social acceptance, and at less cost to the state (Gunningham and Grabosky, 1999). This approach resonates with the broader transition in the role of governments internationally: from 'rowing the boat to steering it' (Osborne and Gaebler, 1992) or choosing to 'regulate at a distance' by acting as facilitators of self- and co-regulation rather than regulating directly. However, its authors caution that there are limits to the circumstances in which it will be possible for escalation up one or more of the three sides of the pyramid.

Meta-regulation takes a somewhat different approach. In its most common manifestation it involves placing responsibility on the regulated enterprises themselves (usually large organisations) to submit their plans to the regulator for approval, with the regulator's role being to risk-manage the risk management of those individual enterprises. This approach has the considerable attraction of being able to engage with complex organisations and complex problems by inducing companies themselves to acquire the specialised skills and knowledge to self-regulate, subject to external scrutiny. As such, this approach is also a form of responsive regulation but it also has links with Smart Regulation in that both of these approaches have the considerable attraction of relieving the state of some of the burden of direct regulation, and of allocating responsibilities to those who may be in a much better position to discharge them (provided they are motivated to do so).

But notwithstanding the appeal of meta-regulation, a receptive corporate culture would seem to be a necessary, albeit not a sufficient condition for its success. Another constraint is that only large and sophisticated organisations will have the resources or capacity to regulate themselves effectively. These are challenging pre-conditions to success and the problems of effective implementation will be greatest when dealing with reluctant compliers, the recalcitrant, or the incompetent.

Unfortunately there are no 'magic bullets' and no single approach that will function efficiently and effectively in relation to all types of enterprises and all circumstances. Nevertheless, some approaches are considerably better than others and there is much to be learnt from each of the regulatory models described above. Their nuanced application in appropriate contexts could considerably advance regulatory compliance and enforcement.

NOTES

1. Instruments are the tools employed by institutions to do what they wish to do.
2. Highly detailed, prescriptive regulation has been the norm in many jurisdictions. The United States in particular has been reluctant to provide discretion to either regulators or business for fear that they might abuse it (see Bardach and Kagan, 1982). The result has been regulation that specifies in very precise terms what duty holders should do and how they should do it, and sets out the specific types of methods (especially technologies) that must be used to achieve compliance in given situations (see generally Gunningham and Johnstone, 1999: ch. 2). Perhaps surprisingly (given standard industry rhetoric against 'command and control' government regulation) some large companies themselves rely on prescriptive internal regulation as one pillar of their efforts to maintain or improve corporate social and environmental performance (Reinhardt, 2000: 157–8).

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