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GOVERNING THE ECONOMY
Markets, Experts, and Citizens

A dissertation presented
by

KAZI SABEEL AL-JALAL RAHMAN

to

THE DEPARTMENT OF GOVERNMENT

in partial fulfillment of the requirements
for the degree of

DOCTOR OF PHILOSOPHY

in the subject of

POLITICAL SCIENCE

HARVARD UNIVERSITY
Cambridge, MA
May 2013

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Dissertation advisor: Professor Michael Sandel (chair) Kazi Sabeel Al-Jalal Rahman

GOVERNING THE ECONOMY
Markets, Experts, and Citizens

ABSTRACT

The 2008 financial crisis provoked a debate over how we as a democratic society ought to govern the modern market economy. Our prevailing response to this problem of economic governance has been to appeal either to free markets as self-regulating, self-optimizing systems, or to technocratic rule by neutral experts. Both these systems are appealing because of they claim to promote the public good free of the corruption, irrationality, conflict, and vagaries of democratic politics. This project aims to overcome this skepticism to sketch an account of a democratic approach to economic governance, inspired by the thought and reforms of the Progressive Era.

I argue below that ideal of democracy should be understood as a matter of political agency: we are free in a democratic society insofar as we experience the challenges and rewards of self-governance. Appeals to markets and experts, from this standpoint, are doubly flawed. Not only to they entrench threats to our individual and collective agency in the form of concentrated private power of firms, diffuse systemic power of markets, and the political authority of unaccountable experts; they also narrow the scope for citizens to experience genuine political agency. This view of democracy as experience highlights prospects for thickening democratic practice that are often overlooked in conventional democratic theories focused on elections, legislatures, and representation. Instead, I suggest that democratic agency can be fostered in three ways: first, through a

reconstruction of regulatory agencies as sites of democracy; second, through an expansion of the role of local governments as another arena in which citizens can engage with the actual practice of governing; and third, through the broadening of economic policy discourses to encompass moral and political, not just technical concerns.

The closing chapters apply these themes to the policy and institutional debates surrounding financial reform. Ultimately, this democratic approach to economic governance suggests a very different response to the financial crisis, pointing to the ways in which current institutions for economic governance can be reworked to foster, rather than supplant, the democratic agency of citizens.

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ACKNOWLEDGEMENTS

Thanks are due first and foremost to my advisors, Eric Beerbohm, Jerry Frug, Nancy Rosenblum, and Michael Sandel for their invaluable support, feedback, and guidance. Most of all, I thank them for providing me the license and encouragement to explore—and for cultivating a commitment to the role that political theory can and ought to play in the world of politics.

I am grateful to a number of interlocutors among the academic community at Harvard, all of whom helped shape the project through conversations and comments on early drafts, especially: David Barron, Dan Carpenter, Akiba Covitz, Christine Desan, Archon Fung, Lani Guinier, Mort Horwitz, James Kloppenberg, Adam Levitin, Martha Minow, David Moss, Tomiko Brown-Nagin, Morgan Ricks, Joe Singer, Richard Tuck, and Adrian Vermeule.

I have also been fortunate for support from a number of research centers and workshops. Thanks are especially due to John Cisternino and the staff of the Tobin Project for fostering a rich interdisciplinary dialogue in Cambridge around the study of democracy and markets. Thanks to the graduate students, faculty, and staff at the Edmond J. Safra Center for Ethics; the Harvard University Center for American Political Studies; the Office of Academic Advising and the Lewis Fellowship program at Harvard Law School; the Government department Political Theory Workshop; and the Harvard Law School Public Law Workshop for providing rich and inspiring forums and support. Andy Rich, Felicia Wong, and the staff at the Roosevelt Institute also provided additional support and opportunities to present findings.

A work such as this is as much a product of a community as of an individual, and I have been fortunate to have found a vibrant community of friends, scholars, and thinkers with whom to share in this journey. I am tremendously grateful for their generosity, their commitment, and their inspiration. This book has largely been written thanks to, because of, and ultimately *for* them, in the hopes that it will help us continue our shared journey. Thanks in particular are due to: Oliver Bevan, Peter Buttigieg, Jonathan Bruno, Josh Cherniss, Tarun Chhabra, Prithvi Datta, Metin Eren, Jeremy Farris, Aaron Greenspan, Michael Lamb, Adam Lebovitz, Yascha Mounk, Justin Mutter, Beth Pearson, Ryan Rippel, Hollie Russon-Gillman, John Santore, Emma Saunders-Hastings, Vaughn Tan, Andrea Tivig, Bernardo Zacka.

I must thank my parents Kazi A. Rahman and Shegufta Rahman, my family Shumona, Laboni, Marc, Leander, and Liam, for their love, support, and the millions of things large and small that they have done and continue to do to help make all of this—and much more—possible. And finally, I thank my partner, Noorain, who I first met before this project started, with whom I am grateful to share life after this work, and to whom I owe more than I can say.

We have frequently printed the word Democracy. Yet …
it is a word the real gist of which still sleeps, quite
unawakened, notwithstanding the resonance and the
many angry tempests out of which its syllables have come,
from pen or tongue. It is a great word, whose
history…remains unwritten, because that history has yet
to be enacted”

— WALT WHITMAN, “DEMOCRATIC VISTAS” (1871)

1 ECONOMIC GOVERNANCE IN AN ANTI-POLITICAL AGE

On a bright but bitterly cold January morning, Barack Hussein Obama ascended the steps of the Capitol balcony to take the oath of office as President of the United States. It was January 2009, and the country was in the depths of the worst economic disaster since the Great Depression. In September 2008, the collapse of the subprime mortgage market had wiped out Lehman Brothers, one of the biggest—and most heavily interconnected—investment banks in the world. Within days, credit had effectively frozen, and the United States was staring down the abyss of the largest financial and economic collapse since 1929. And yet in the midst of the crisis, the mood in January 2009 was hopeful, even buoyant, with the promise of a new beginning. Obama cast himself as speaking to the extraordinary socioeconomic challenges of the day. In his inaugural address, Obama outlined the challenges facing the country as a stirring call to action:

> Time and again these men and women struggled and sacrificed and worked till their hands were raw so that we may live a better life. They saw America as bigger than the sum of our individual ambitions; greater than all the differences of birth or wealth or faction. This is the journey that we continue today. … Starting today we must pick ourselves up, dust ourselves, off, and begin again the work of remaking America.[1]

[1] Barack Obama, Inaugural Address, January 20, 2009.

If there was a central theme to the Obama candidacy, it was this: that collectively, we as citizens of a democratic America could band together and remake our world, shape our destiny, and renew our sense of civic engagement and empowerment.[2]

It was a powerful argument, and understandably resonant. The economic crisis undermined decades of faith in the self-correcting and growth-promoting nature of financial markets. But while new economic policies seemed called for, the loss of our ability as citizens to control and shape our own economic fate—and to hold our own government accountable and responsive—limited our ability to respond to changing economic conditions. Obama's appeal at the height of the 2008-9 collapse was, correctly, to identify the economic crisis as fundamentally a problem of politics. Economic threats like instability, financial risk, unemployment, and opportunity are the central stuff of democratic politics, integral to realizing any aspiration to a just society and a meaningful life for all citizens. Without a responsive and accountable political system, we lack the means to respond to the economic challenges of the day. By calling upon the hope of renewed civic engagement, Obama suggested that we as citizens could both retake control of our government and, in so doing, respond to the severity of the economic crisis itself.

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[2] See e.g., Barack Obama, remarks upon clinching the Democratic nomination for President, St. Paul, MN, June 3, 2008: "The journey will be difficult. The road will be long. I face this challenge with profound humility, and knowledge of my own limitations. But I also face it with limitless faith in the capacity of the American people. Because if we are willing to work for it, and fight for it, and believe in it, then I am absolutely certain that generations from now, we will be able to look back and tell our children that this was the moment when we began to provide care for the sick and good jobs to the jobless; this was the moment when the rise of the oceans began to slow and our planet began to heal; this was the moment when we ended a war and secured our nation and restored our image as the last, best hope on Earth. This was the moment - this was the time - when we came together to remake this great nation so that it may always reflect our very best selves, and our highest ideals."

This vision of democratic renewal, however, evaporated relatively quickly. The debate over post-crisis financial reform policy is emblematic. While the crisis itself provoked widespread popular anger against the malfeasance of Wall Street firms, growing inequality exemplified by extravagant CEO pay packages, and the failures of regulators themselves, the actual policy outcome of the debate over financial regulation, the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010,[3] spurned these populist overtones. The Act provided regulators at the Federal Reserve Bank, the Securities and Exchange Commission, and other bodies with greater authority, resources, and a mandate to coordinate their regulatory activities and prevent future financial crises. These policy prescriptions of Dodd-Frank—as with the other major economic reform initiatives of the Obama administration—were not only a product of legislative politicking and maneuvering; rather they manifested an underlying theory of economy, democracy, and government. Dodd-Frank exemplifies a classic New Deal-inspired faith in expert economic governance. Financial markets are complex creatures upon which the rest of the economy depends; their management and optimization therefore cannot be left to the whims of the lay public, the direct commands of representatives in Congress, nor to the vagaries of market forces. It is only through delegating greater authority to politically-insulated regulators, in this view, that the complexity of the modern economy can be appropriately managed for the public good.

This managerial, expert-led approach seems on the surface to offer the best of all worlds. Through fine-tuned expert management, we can ensure that we

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[3] Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203 (2010).

harness the benefits of modern financial innovations and the market economy, while mitigating its worst excesses. These experts in turn operate in the name of the public good, without falling prey to the pressures and frictions of ordinary democratic politics. Yet on both left and right, there is a continued, if not growing, unease about the degree to which such expert regulators can or should play such an authoritative role in the governing of the modern economy, however complex it may be. These concerns speak to some very real economic and political dangers that come with the turn to expertise. Consider the following instances.

To address the threat of "too-big-to-fail" (TBTF) financial firms like Lehman Brothers from sparking another economic crisis by their collapse, Dodd-Frank creates an elite Financial Stability Oversight Council (FSOC) comprised of the heads of the major financial regulatory agencies tasked with devising a formula to identify TBTF firms and regulate them accordingly. In the years since Dodd-Frank's passage, however, the FSOC has struggled to develop such a formula. How big is "too big"? What kinds of economic harms count—financial harms to the stock market, or downstream effects on employment?[4] Deciding these questions implicates more than just technical considerations; moral and political judgments about the distribution of harms and protections are also at stake. Yet these are judgments that regulators at the Fed or elsewhere are ill-suited to make, however expert they may be.

Meanwhile, in the emphasis on expert judgment, our institutions for economic regulation have also been built to privilege centralized, expert-led institutions, systematically undermining the scope for democratic citizen

[4] See generally, Adam Levitin, "In Defense of Bailouts," *Georgetown Law Journal* 99 (2011), 435-514.

engagement and divesting citizens of meaningful roles in shaping financial policies. But despite—or arguably because of—such insulation, these technocratic institutions have just as often worked to serve industry over public interests. One key provision in Dodd-Frank institutes what is known as the Volcker rule, a ban on proprietary trading that attempts to prevent the kind of risky bets fueled the boom and collapse of mortgage-backed securities during the crisis. But as regulators have worked to draft and implement the actual rule itself, industry groups have successfully lobbied aggressively to include a variety of exceptions that have neutered the impact of the rule. By contrast, consumer and other advocacy groups pushing for a more aggressive rule have had a much harder time making their voices heard.[5] Similarly, federal regulators prior to the crisis overruled the efforts by several local governments like the city of Oakland to address the growing predatory lending and foreclosure crisis before the collapse of the subprime mortgage market.[6] The result was to leave lenders with a free hand, in the name of ensuring a uniform national scheme of lending regulations. Although the eventual crisis vindicated these early reform efforts by cities, Dodd-Frank and federal regulators have continued to trump such local initiatives.[7]

The market economy is at the heart of many of the most central moral concerns we face as a society: concerns about distribution, welfare, opportunity, and the good life. It is therefore also a central concern for us as citizens in a

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[5] See Jesse Eisinger, "The Volcker Rule, Made Bloated and Weak," *New York Times* Dealbook, February 22, 2012; Floyd Norris, "Bank Rules That Serve Two Masters," *New York Times*, October 13, 2011.

[6] See e.g., *American Financial Services Association v. City of Oakland*, 34 Cal.4th 1239 (Cal. 2005).

[7] Comptroller of the Currency, letter to Senator Thomas Carper, May 12, 2011 [on file with author].

democratic polity. Yet our contemporary institutions for economic governance are distrustful of the role of the citizen, keeping them at arm's length, preferring instead the more efficacious machinations of the market system or expert regulation.

It wasn't always this way. A century ago, financial crises were the central stuff of mass social movements. In the midst of an industrializing economy afflicted by booming inequality and widespread social and economic dislocation, anger over the economic and political power of finance animated some of the largest mass social movements in American history. For both the rural Populist movement of the late nineteenth century and the urban social reform Progressive movement of the turn of the century, finance served as a central villain against which reformers mobilized. Finance, led by prominent elites like J. P. Morgan, represented the worst excesses of the new economy: incentivizing speculation and gambling; driving growing inequality as bankers expanded their growing wealth by hijacking and co-opting the use of other people's money; corrupting the political process itself as these economic elites leveraged their wealth to influence legislatures and protect their own interests. These mass movements advocated a variety of economic, social, and political reforms from redistribution to price controls to antitrust measures to the socialization of the financial system itself. They also shared a common conviction that it was through the mobilization and power of the people themselves that the economic and political domination of these elites would be broken.

Though the specific proposals of these turn of the century reformers may not be directly applicable today, this ethic of seeking a specifically democratic response to the moral challenges of the market economy is instructive for us today.

In this project, I argue that instead of turning to neutral, expert regulators to optimally manage the market economy, we ought to look to our own capacities as democratic citizens. We the people must govern our own economy. To do so we must also expand our normative ideals of what democracy means and how it can be institutionalized. As such, this project does argue against the laissez-faire tradition of rejecting state regulation and favoring markets as self-correcting. But the most central opponent in this project is the technocratic approach of responding to market failures through expert-led governance exemplified by Obama and the tradition of New Deal progressivism. The following chapters develop a view of democratic economic governance building on four central arguments.

First, although such economic policy debates are often caricatured as debates of “more” versus “less” state intervention in the free market, these debates are actually driven by a more nuanced clash between rival conceptions of economic governance. These conceptions of economic governance combine two components: a moral view of freedom and the relationship between the state and the economy, and an institutional concern about protecting such systems of ordering the economy from the threat of corruption, special interest influence, or capture. The laissez-faire argument, therefore, is more than just a claim of freedom from all types of state interference. Rather, it also rests on a view that markets are also less prone to capture by special interests because of their diffuse and decentralized nature. This concern with corruption explains the resilience of laissez-faire thought, for the laissez-faire argument rests partly on an institutional sociology that critiques state institutions as prone to capture, while markets as decentralized aggregative systems are less prone to such special interest influence.

This dual nature of the laissez-faire argument also explains the brittleness of the technocratic argument against free markets. While it may be true that flaws and failures of market society call for greater state regulation, the case for such regulation too often rests on a faith that experts themselves are robust to corruption or special interest influence—a faith that has been shaken in recent decades among both liberals and conservatives. This understanding of the debate between laissez-faire and technocratic views of economic governance points to the need for a third alternative view—a more democratic alternative that responds to both the limitations of free markets and of expert regulators.

Second, markets and experts claim to act as apolitical, neutral, and rational modes of optimizing the economic order. The turn to markets and experts speaks to a deep-seated unease with the tumult, conflict, and disagreement endemic in ordinary democratic politics. This unease motivates us to transfer more and more decisions outside of the realm of democracy to markets or experts. But this appeal of markets and experts is illusory, obscuring realities of power, politics, and moral controversy that operate beneath the veneer of market-based or expert-led efficiency. Instead of responding to these concerns about democratic politics by narrowing its scope, we should instead seek ways to expand its vibrancy, making it more accessible and channeling democratic contest in more productive ways.

Third, developing such a view of democracy requires that we expand our normative understanding of the ideal itself. I argue that we must view democracy not as the registering of preferences, the selection of representatives, or even simply deliberation over the common good. Rather, all of these elements are components of a broader democratic commitment to expanding the *capacities* of citizens to engage in the actual *experience* of governing. It is only when we possess the

political agency to engage in meaningful decision-making—and to live with and learn from the consequences of those decisions—that we can lay claim to the mantle of democracy.

Fourth, we require a diverse array of institutional structures and conditions in order to realize this kind of democratic political agency. While elections, plebiscites, and legislatures have long had a pride of place in democratic theory, I suggest that thickening our democratic capacities and experience requires that we turn instead to front-line institutions of governance such as regulatory agencies and municipal governments. These institutions lie at the interface between state and society, where the actual practice of devising final governmental policies and regulations takes place. It is here that citizens can be engaged in a more meaningful and empowered mode of participation.

The rest of this introduction elaborates each of these themes.

Markets, experts, and citizens

In the spring of 1945, Friedrich Hayek journeyed to the United States to give a hastily-arranged lecture tour arranged in light of the surprising and escalating success of his recently published critique of central planning, the *Road to Serfdom*. After failing to even find a publisher in Europe, Hayek's book—particularly its abridged version in *Reader's Digest*—became wildly popular. Conservative writers and activists appropriated Hayek's argument in their own critique of Franklin Roosevelt's New Deal. Yet Hayek himself was dismayed by this characterization of his work as an anti-government creed; his own view was in fact much more nuanced, including support for an extensive role for the state in

managing market downturns, investing in infrastructure, and providing forms of social insurance.[8] Indeed, Hayek's critique of the state and his defense of the market rested on a dual foundation: not just a commitment to a negative understanding of liberty as the freedom from interference, but also a preference for markets as epistemically superior institutions for organizing collective life. Centralized regulators, Hayek feared, could never possess all the necessary information to make socially optimal choices for allocating resources; it was only the diffuse and decentralized system of the market that possessed the capacity to aggregate and harness the multiplicity of local individual preferences and understandings in a coherent manner.[9] Although at the time Hayek saw himself as part of an endangered minority of classical liberals eclipsed by the rise of Keynesianism and growing faith in the modern regulatory state, his ideas would go on to inspire the resurgence of laissez-faire thought through his influence on the next generation of conservative thinkers like Milton Friedman, and the ecology of free-market advocacy groups, businesses, and think-tanks.[10] Hayek's account also resonated with the kinds of concerns that animated pre-New Deal understandings of the markets, and critiques of early efforts to build economic regulatory

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[8] Angus Burgin, *The Great Persuasion: Reinventing Free Markets since the Depression* (Cambridge: Harvard University Press, 2012), 87-91.

[9] See e.g., Friedrich von Hayek, "The Use of Knowledge in Society," in Chiaki Nishiyama and Kurt Leube, eds., *The Essence of Hayek* (Stanford: Hoover Institution Press, 1984), 211–24.

[10] See generally, Burgin, *The Great Persuasion*, and Kim Phillips-Fein, *Invisible Hands: The Making of the Conservative Movement from the New Deal to Reagan* (New York: WW Norton, 2009).

institutions in domains such as labor, railroad and antitrust policy during the late nineteenth and early twentieth centuries.[11]

Hayek's account distils a tradition of laissez-faire thought in American politics that bookended the New Deal era. The laissez-faire view of economic governance, that economic order is best achieved through "free markets" untroubled by state intervention, has served as the primary intellectual critique of reformed or expanded state regulation of the economy. As Hayek's own account suggests, laissez-faire economic governance is not the kind of blanket rejection of the state or valorization of the market as it is often caricatured. Rather, the idea of laissez-faire draws its force from two sources. The first is a normative view of freedom as non-interference. This commitment to negative liberty valorizes the autonomy of individuals to form contracts and make their own decisions free of external interference from other individuals or from the state. The second is a particular concern that state political power can be co-opted to serve the purposes of particular interests rather than promoting the general welfare. For laissez-faire, the commitment to negative liberty emerges in part as a bulwark against such corruption or capture.

These moral and institutional concerns are what animate laissez-faire's distrust of the state and preference for the market. As a moral matter, the market seems to better track a normative commitment to unrestrained individual autonomy, whereas state power—beyond that which is minimally required to ensure property and contract rights and protect against external threats—poses a threat to such individual autonomy. As an institutional matter, the ability of

[11] See e.g., Howard Gillman, *The Constitution Besieged: The Rise and Demise of Lochner Era Police Powers Jurisprudence* (Durham: Duke University Press, 1993).

markets to aggregate information, allocate resources, and respond to changes in the costs, availability, and preferences over particular resources makes them more dynamic, adaptable, and ultimately robust to corruption or capture when compared to centralized political institutions like the state. The market is thus a self-equilibriating, optimizing, and adaptable institution for managing economic order more effectively than relying on fallible and corruptible individual political leaders or policymakers. In this way, laissez-faire represents a kind of anti-politics: the problem is not the existence of the state itself, but rather the proclivity of politics to tend towards corruption, inefficiency, and chaos. By contrast a decentralized aggregative system like the market can absorb the myriad of individual desires and actions and produce socially optimal allocations.

This multidimensional quality of the idea of laissez-faire explains its persistent impact as the driving force behind major periods of reform and advocacy. The rejection of Progressive Era attempts to achieve minimum wages or workday regulations, for example, appealed not only to a narrower view of freedom, but also to the concern that expanded regulation might serve the partial and particular interest of a certain social class rather than the general welfare. Similarly, the turn to deregulation in the late twentieth century gained traction not only because of its appeal to the market, but also because of the growing concerns that the regulatory institutions of the New Deal state were prone to corruption, capture, inefficiency, and unaccountability.

It was this very appeal to expert regulators that comprised the heart of New Deal and more contemporary efforts to expand economic regulation. In the late 1930s, despite the ongoing Great Depression, a new generation of policymakers began to envision an unprecedented mastery over the vagaries of the market

economy. Speaking at Yale University in 1938, James Landis gave what remains one of the most assertive defenses of the modern administrative and regulatory state. A leading figure in Franklin Roosevelt's brain trust and one of the chief architects of the newly-created Securities and Exchange Commission, which he would later chair, Landis outlined in his lectures a full-throated defense of this technocratic vision of economic governance. The challenges of the modern industrial economy, for Landis, required new institutions to manage the vagaries of the market system; the market could not be relied on to produce a socially optimal economic order on its own. But Landis was equally critical of the "inadequacy" of traditional institutions of governance: neither Congress nor the courts possessed the knowledge or deliberative capacities to make such complex economic policies.[12] Such a task demanded the expert hand of regulators positioned in institutions like the SEC, insulated from the day-to-day pressures of democratic politics. The professionalism, expertise, and transparency of regulatory policy would, according to Landis, be more than sufficient to ensure that the regulators employed their vast authority for the public good.

Just as Hayek captured an idea of laissez-faire that manifested throughout the modern era as a critique of the state, Landis' account captures in its most aggressive form the technocratic vision of economic governance, from Progressive Era thinkers like Charles Francis Adams to New Dealers like James Landis, to contemporary advocates of the regulatory state like Stephen Breyer and Cass Sunstein. This technocratic approach to economic governance embodies a commitment to a more active role for government in the economy: not just in

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[12] James Landis, *The Administrative Process* (New Haven: Yale University Press, 1938), 70.

ensuring basic rights of property and contract, but also in correcting market failures, mitigating risks, and protecting vulnerable populations through public policies, social insurance schemes, and other kinds of regulation. As with laissez-faire, the technocratic view of economic governance combines a moral and an institutional claim. As a moral matter, technocratic economic governance often rests on a broader view of freedom as involving not only the protection from political or state interference, but also from other kinds of private or systemic coercion that may infringe on an individual's autonomy. From this standpoint, state intervention may in fact be freedom-enhancing. As an institutional matter, the technocratic view doubts that disaggregated and decentralized institutions like the market can on their own yield socially optimal economic allocations and arrangements. Rather, the public good requires the creation of specialized institutions where uniquely expert or talented policymakers can, through the judicious use of their knowledge and public-spiritedness, craft regulations so as to promote the public good. This institutional vision calls for economic policy to be made through bodies that are centralized, expert-led, and politically-insulated, free to make policy on the basis of morally neutral scientific knowledge.

Despite their opposition to the laissez-faire distrust of the state and valorization of markets, these technocratic thinkers share with laissez-faire a habitual unease with democratic politics. Indeed, the appeal to expertise is in part a way to defend the substantive goals of government regulation of the market, while sidestepping the anxieties about democratic corruption, chaos, and unresponsiveness. If governmental activity can be channeled through insulated, neutral, expert, and public-spirited regulators, the traditional concerns about dangers of political power can be addressed without having to resort to the laissez-

faire extreme of 'free markets'. This shared unease with democratic politics, however, introduces a fundamental tension at the heart of the technocratic account. On the one hand, technocratic economic governance draws its moral force from a critique of market society and an appeal to the importance of political institutions to promote the public good. On the other hand, this distrust of ordinary democratic politics leads the idea of technocracy to commit to a particular institutional form for achieving economic order: the insulated expert regulator or elite policymaker. As a result, technocratic economic governance is highly dependent on faith in expertise for its legitimacy. Yet this faith is exactly what laissez-faire denies: the notion that individuals wielding political power can be reconciled with individual freedom and can act effectively, responsibly for the public good, rather than being captured or subverted by private interests. For all its virtues, the idea of technocracy is therefore surprisingly brittle, for it is uniquely vulnerable to the criticisms of laissez-faire.

It is therefore unsurprising that so much of the debate around economic governance in recent years has revolved around this basic clash between laissez-faire and technocratic views of economic governance. But these are not the only two possible approaches to the problem of managing the modern economy. Even as New Dealers like Landis worked to realize their vision of economic governance through rational, neutral expertise, there remained a different reformist tradition, one that shared the technocratic critique of the market, but looked not to experts but to citizens as the solution. Writing not long before Landis' own lectures, Supreme Court Justice Louis Brandeis, a veteran and central intellectual figure of the Progressive movement, took the same starting point as Landis: that the severe economic crisis of the Great Depression called for some form of expansive policy

response. But for Brandeis this challenge pointed not to the role of experts but rather to citizens. Echoing Hayekian critiques of the aspiration to technocratic mastery, Brandeis warned that formulating the perfect rational economic policies would require "some measure of prophecy," yet "man is weak and his judgment is at best fallible." But where for Hayek and laissez-faire critics such fallibility would be sufficient to turn back to the market as a preferred institution for economic governance, Brandeis turned instead to the ideal of democracy: democratic politics, for Brandeis, was crucial to allow for policy innovation, experimentation, and social learning over time.[13] Not only was this the best institutional arrangement for yielding policy responses to the dangers of market society; it also represented a moral imperative for "only through participation by the many in their responsibilities and determinations of business can Americans secure the moral and intellectual development which is essential to the maintenance of liberty," and thus remain "masters of their own destiny."[14]

Thus, where the technocratic vision responds to the problems of the market through centralized, expert-led, morally neutral policy processes, this democratic vision instead appeals to the idea of multiplying the sites and spaces for democratic policymaking, facilitating participation and innovation. It also sees the problems of economic governance not just as matters of rational economic management or optimization, but also as deeply moral and political problems of hardship, dislocation, inequality, and disparities of power. Similarly, this democratic approach suggests a view of freedom that, while sharing with the technocratic

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[13] *New State Ice Co. v. Liebmann*, 285 U.S. 263 (1934) (J. Brandeis, dissenting), at 310-11.

[14] *Liggett v. Lee*, 283 U.S. 517 (1932) (J. Brandeis, dissenting), at 580.

account the idea that state interference can be freedom-enhancing by mitigating harms emerging in the private and economic arena, goes still one step further through its commitment that such state action be the product of a fundamentally democratic process. It is not enough that these policies promote a common good by responding to the harms of the market; these policies must themselves be constituted by the active engagement of citizens themselves.

There are therefore three distinct approaches to economic governance: laissez-faire, technocratic, and democratic. Laissez-faire economic governance emphasizes markets as self-optimizing institutions, to be left free of state interference as a way to avoid the dangers of corruption and unaccountable state authority. Technocratic economic governance relies on insulated experts to develop market-optimizing policies. This institutional structure allows technocrats to respond to the problems of markets while avoiding the perceived dangers of democratic politics. The third alternative of democratic economic governance offers a way to address the weaknesses of both laissez-faire and technocracy: it shares with laissez-faire a skepticism of expert authority, and with technocracy a critique of markets. But unlike both laissez-faire and technocracy, this democratic approach responds to the problems of markets and state authority by seeking ways to expand the political capacities of citizens, empowering them to engage in the morally- and politically-charged decisions of economic policy. This democratic view, therefore, is distinguished by its embrace of politics, in contrast to both markets and experts which seek to avoid the tumult of political disagreement by depoliticizing economic governance, moving it out of the domain of democratic politics into the domain of supposedly neutral and frictionless market forces or expert management.

A central theme of this project, therefore, is the recovery and development of this democratic vision as an alternative response to critiques of both the market and expertise. Indeed, this cleavage between democratic and technocratic responses to the market has been a crucial one throughout economic reform movements, from the Progressive Era to the present. One of the goals of this project is to bolster this democratic alternative to technocratic regulation.

Mapping the debates over economic governance in this way highlights two important points. First, economic governance is not just about normative ideals of freedom; it is a more nuanced comparative institutional question about what social institutions are more likely to be robust to corruption and to produce socially optimal decisions. The appeal of both markets and experts lies in their proclaimed capacity to produce neutral, rational economic orderings free of the vagaries of democratic politics. Yet at the same time, the technocratic account is on shaky ground because of its reliance on faith in expertise—a faith that is easily shaken. Second, if our task is to develop a more democratic alternative to both markets and experts, we need to do more than simply advert to the ideal of "the people". We need instead to offer an institutionally-rich account of how democracy can produce effective economic governance, and do so in a way that is responsive to the citizenry, and less prone to corruption, capture, or subversion. The project of restoring a more democratic vision of economic governance is as much about defusing the laissez-faire appeal to markets as it is about challenging the more recent tradition of technocratic economic governance, which has for decades dominated efforts to respond to the problems of the market economy. Such an effort must overcome the deep distrust and suspicion of democratic politics shared

by the laissez-faire and technocratic accounts—a distrust that has become increasingly entrenched in our popular discourse and politics.

The false hope of anti-politics

For mainstream reformers responding to the financial crisis, the failures of the market seemed like a final winning argument in defense of the modern regulatory state. The persisting anxieties about regulation and expert accountability, for these reformers, is a product of our changing attitudes about the state. Where Franklin Roosevelt inherited a robust debate from turn of the century critiques of modern industrial capitalism and reformists' efforts to expand the role of government and social organization in response, Obama entered into a very different conversation, one that had come to revolve around the libertarian and conservative attack on the very idea of effective and accountable government action, alongside ongoing efforts to valorize the efficiency and desirability of free markets. "The question on the New Dealers' minds, however naively they sometimes answered it, was how best to articulate social action and individual energy to promote the welfare of all," writes historian Daniel Rogers. "By contrast, Obama inherited four decades of public discussion in which the importance of society has steadily diminished in favor of individual choice, personal identities, markets in goods, and markets in selves. This time the ideas with the loudest megaphones came not from the solidaristic left but the libertarian right."[15]

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[15] Daniel Rogers, "'Moocher Class' Warfare" *Democracy Journal* (Spring 2012), 84-90, at 85.

By itself, this shift in background support for government between 1932 and 2009 does not, however, fully explain the pervasive skepticism and unease with the appeal to economic expertise of the kind exemplified by Dodd-Frank. Rodgers—and many other critics of the limited vision of the Obama era response to the crisis—are right to cast the problem as a deeper matter of ideas, and they are right to point to a shift in the overarching ethos of the era, from a focus on innovating government responses to the failures of the market in the early New Deal to a focus on restraining government excess in the politics of post-Reagan America. But this standard critique is misleading because it gives too little responsibility to the failures *within* the New Deal-inspired vision of government itself. Obama's approach to the economic crisis, as with the New Dealers in whose footsteps he follows, is morally flawed in its own right, for it rests on a willful preference for expertise over democracy. The conservative critiques of the regulatory state do in fact pick up on a very real and legitimate concern over the accountability, responsiveness, and efficacy of such expert-driven regulation. In responding to the problems of an alien, threatening, uncontrollable market economy, we have turned to an equally alien, threatening, and uncontrollable system of expert regulation, too far removed from the control and agency of the people themselves to generate the kind of broad-based legitimacy needed to survive. The financial crisis, then, did not only reveal weaknesses in the appeals to the self-correcting market. It also revealed a broader, more disturbing pattern in contemporary politics: the degree to which even reformers on the left seem to distrust the basic idea of democracy itself.

In the country that claims democracy as its birthright, it is remarkable how widespread and deep-seated a sense of democratic failure has become. In recent

years, hopes for social progress have come *not* from the democratic political system—where politicians and legislatures are held in nearly universal contempt—but from just about every other avenue: appeals to the innovation of businesspeople and entrepreneurs; the wonders of the free market, privatization and deregulation; the promise of non-governmental civil society organizations, social entrepreneurs, or mega-philanthropies; the reliance on neutral, scientific expertise. From outsourcing and government contracting, to the valorization of social entrepreneurship as modes of collective problem-solving, we live in an era where it is private, business, and expert initiative, rather than the collective political capacities of us as citizens and groups, that seems to offer the most attractive route to managing and solving social problems. The preference for experts and markets is just one manifestation of this broader pattern. What all these diverse alternative modes of social reform share is a common distrust of democratic politics, and therefore a similar quest for depoliticized modes of addressing social problems. Democracy seems too unsophisticated to develop nuanced public policies, too subject to deadlock and hyper partisanship, too vulnerable to interest group politics and capture, too prone to incoherence and chaos. Elections are too unwieldy, too partisan; popular protests when they do take place are viewed with distrust as ill-conceived at best, and pathological at worst.

This distaste for democratic politics is at the heart of the appeal of markets and experts as systems of economic governance. Markets present themselves as natural forces to which we as individuals must adapt; they are driven by laws of nature beyond the reach of human agency. This makes them apolitical—or even anti-political: immune to alteration, lobbying, or corruption, and therefore more

reliable as guarantors of social welfare. Technocracy presents itself in a similar manner: by removing policy decisions from the reach of democratic politics, technocracy depoliticizes these issues, immunizes them from democratic contest, and in so doing achieves the necessary latitude to make socially-optimal policy decisions on the basis of rationality rather than politics. In these accounts, democracy recedes into the background, at worst rejected outright; at best, relegated to the status of a distant authorizer or delegator of authority to the more effective system of free markets or regulatory agencies.

But the appeal of markets and experts as more rational, effective organizers of the economy is ultimately illusory. Markets are not neutral, frictionless optimizers of economic order; rather, they are domains of power and conflict, riven by inequalities in bargaining power, welfare, and position, and prone to all sorts of distortions and failures. Similarly, technocratic policymaking is inextricably bound up in political and moral judgments that inevitably shape the application of supposedly neutral expertise. Turning to markets and experts as our preferred modes of economic governance does not eliminate these concerns of power, politics, and morality; it submerges them from view, out of reach. This in turn undermines our ability to act as democratic citizens, and to address the very pathologies of markets and expertise in economic policymaking.

Markets and technocracy sterilize economic governance, removing it from the scope of our collective agency. This makes their failures particularly difficult to undo, overcome, or revise. It is no wonder we tend to view the market as a force of nature, prone to tempests and shocks that we must simply weather. Nor is it a surprise that the technocratic state is so easily vilified as an alien imposition. Both market forces and technocratic regulation are the product of rules, laws, and

systems that we as political actors have sanctioned, but we have done so in ways that deliberately removes these systems from our own control, out of a distrust of the chaos and corruption that is likely to result from such political involvement in the managing of the economy. By cordoning off more and more policy space away from the reach of either democracy or politics, the laissez-faire and technocratic approaches arrogate ever more authority to a set of institutions held at arms-length from ordinary channels of democratic politics: the market, and the expert regulatory agency. It also over time contributes to an accelerating emaciation of the domain of democratic politics, as the central issues of political debate are increasingly reallocated from the domain of democratic decision-making to the domain of the neutral, optimizing market, or the realm of technocratic expertise.

Caught between the anti-politics of the 'free market' and the anti-politics of technocratic regulation, it is little wonder that our received conceptions of democratic vibrancy have little traction in contemporary politics and discourse. As Dana Villa laments, "what can 'the public' and political institutions be in a world so dramatically constrained by the imperatives of the global marketplace and the ubiquity of bureaucratic hierarchy and bureaucratic process?"[16] Put another way, how can we have democracy, in any meaningful sense of the term, in a complex modern society driven by the imperatives of the market, or managed through the insulated authority of the regulatory bureaucracy?

The biggest challenge to envisioning a more democratic approach to economic governance is overcoming this pervasive sense of impossibility. Critics of democratic politics tend to compare a particularly non-ideal account of democratic

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[16] Dana Villa, *Public Freedom* (Princeton: Princeton University Press, 2008), 25.

politics with a rosy view of democracy's alternatives—whether it is the free market or the virtuous expert regulator. While the current weaknesses of democratic functioning—from disparities in political voice and representation to defects in the basic electoral system of voting, campaign financing, and the like—cannot be ignored, these limitations should compel us not to abandon or restrict democratic politics, but to expand and revive it. The failures of contemporary democracy are the results of a particularly emaciated set of democratic institutions and practices; absent the kind of institutional support and structure needed to foster effective and meaningful democratic engagement, it is no wonder that democratic politics seems unproductive and ineffective. Democracy, for all its failings, ultimately offers greater hope for responsiveness, adaptability, and accountability.

But to realize this hope, democracy must be understood not as the transmission of citizen preferences through elections, but rather as a set of practices and institutions that expand our capacities as individuals and collectives to remake our world through the common project of engaging in politics. Too often both critics and proponents of democratic revival rest on mostly conventional understandings of democracy as requiring the transmission of individual preferences through elections of representatives or policymakers, who are then empowered to act in accordance with the public good. This basic electoralist understanding of democracy has its strengths. It describes a good deal of the modern experience of democracy, and it points towards several important avenues for democratic reform, such as campaign finance restrictions and combating voting rights violations. But it also overlooks the wider range of institutional forms that can help contribute to a vibrant democratic polity. Democracy relies not only on elections, but on other sites of democratic action,

including the very regulatory agencies that are at the heart of many of the anxieties over the modern regulatory state.

Democracy as experience

The impulse to sterilize democratic politics by appeal to markets and expertise picks up on a widespread latent anxiety about democracy: that relying on the rule of the people may be incoherent, chaotic, prone to the passions of the multitude. This is a long-standing anxiety about democracy. Indeed, recent efforts to reimagine the scope and effectiveness of democracy have focused on the epistemic qualities of democratic governance, finding ways that the collective wisdom of the crowd can be harnessed to supplement, complement, and even rival the supposed epistemic strengths of the free market or technocratic expertise.[17] But I argue for a broader and thicker view of democracy, not as the generation of information, but rather as the fostering of the *experience* of governing.

Where many other contemporary efforts at democracy reform emphasize the creation of deliberative, collaborative, and transparent governmental processes,[18] this focus on democracy as experience sees the key feature of democracy is not the aggregation of individual preferences or the expression of a unified collective will, but rather its capacity for fostering ongoing political contest, debate, and the development of ideas and politics over time. The vibrancy of such

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[17] See e.g., David Estlund, *Democratic Authority: A Philosophical Framework* (Princeton: Princeton University Press, 2008); Helene Landemore and Jon Elster, eds., *Collective Wisdom: Principles and Mechanisms* (New York: Cambridge University Press, 2012).

[18] See e.g., James Fishkin, *When the People Speak: Deliberative Democracy and Public Consultation* (Oxford: Oxford University Press, 2009).

a democracy is determined by the degree to which citizens can directly engage in and experience the challenges, difficulties, and rewards of collectively determining their own fate. Rather than displacing the real business of governing to seemingly better institutions of markets or expertise, this view of democracy would instead focus on expanding the opportunities for citizens to experience self-rule—and in so doing, expand their capacities for moral judgment and learning over time. This approach then does not focus on getting democratic politics to produce the "right" policy answers; rather it focuses on empowering us as citizens to govern ourselves, to debate our visions of what a good society looks like—and equally importantly to face and learn from mistakes we might make.

This focus on the experience of democracy points towards a substantive set of concerns for public policy. In this view, the biggest moral threats in a democratic society are those practices and arrangements that undermine the capacities and powers of citizens to be active political agents: the concentrated private power of firms who can dominate individuals in the economy; the diffused system of the market that can narrow one's life opportunities and prospects; the specter of an unresponsive and unaccountable state itself. All of these types of power create challenges to the idea that citizens should be the primary agents in shaping their own economic and political destiny.

More importantly, the idea of democracy as experience also implies a participatory view of democratic politics, underscoring the value of institutional structures that can make participation more possible, and productive. Without the ability to act—whether by proposing policies, sharing in implementation, or initiating challenges to existing practices—citizens cannot meaningfully partake in

the practice of self-government.[19] This participatory ideal is much maligned. But as Carole Pateman argues, "neither the demands for more participation, nor the theory of participatory democracy itself, are based, as is so frequently claimed, on dangerous illusions or on an outmoded and unrealistic theoretical foundation. We can still have a modern, viable theory of democracy which retains the notion of participation at its heart." To fail to achieve this is not indicative of democracy's failings, but is rather a "failure of the political and sociological imagination" of democratic theorists.[20] Equally importantly, this kind of direct participation in the practice of political judgment is necessarily contestatory; it will not necessarily nor should it ideally produce a genteel consensus among participants. Without some form of public discussion, debate, and judgment, such political action would be reduced to simple exercises of power. Such debate must necessarily involve disagreement, passion, and argument, but it provides a route towards gradual emergence of considered judgments and common understandings through debate and experiment.[21]

A vibrant democracy is thus one that facilitates, structures, and channels political disagreement in productive ways. The central problematic for democratic theory, then, is not so much the problem of disagreement, but rather the problems

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[19] See e.g. Patchen Markell, "The Rule of the People: Arendt, Arche, and Democracy," *American Political Science Review*, 100:1 (2006), 1-14.

[20] Carole Pateman, *Participation and Democratic Theory* (Cambridge: Cambridge University Press, 1970), 111.

[21] See e.g. Brian Garsten, *Saving Persuasion: A Defense of Rhetoric and Judgment* (Cambridge: Harvard University Press, 2006), 86-196.

of demobilization, sclerosis, and imbalances of political power.[22] The "most fundamental threat to democratic political activity," therefore, "lies in the loss of responsiveness to events: the erosion of the contexts in which action makes sense."[23] Responding to these problems of demobilization, depoliticization, and disempowerment requires a reworking of democratic institutions so that they work particularly to catalyze and foster political action. Sustaining citizen engagement with politics requires that we "care for the public world," that we "create and preserve a set of laws, institutions, and public spaces that make active citizenship possible."[24]

What does this vision of a participatory, contestatory democratic political agency look like in practice? How can it be realized? Overcoming the anxieties of democratic dysfunction requires more than a theory of democracy; it also requires a concrete vision of how these normative ideals can be achieved. The account of democratic political agency explored in this project suggests that meaningful democracy requires open moral debate, contestation, and judgment. This in turn suggests that we need institutions to house and foster this discussion, to enable citizens to engage and to make such contestation productive. The ability of both associations and individuals to engage in meaningful democratic participation depends on the institutional and discursive context in which policies are decided; changes to these contexts can magnify the abilities of citizens and associations to

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[22] William Simon, "Three Limitations of Deliberative Democracy," in Stephen Macedo, ed., *Deliberative Politics: Essays on Democracy and Disagreement* (Oxford: Oxford University Press, 1999), 49-57, at 52.

[23] Markell, "The Rule of the People," 12.

[24] Villa, *Public Freedom*, 347.

engage and thereby experience and exercise real political power. It is exactly these kinds of spaces for democratic political action that free market and technocratic frameworks of economic regulation seek to eliminate by creating a distance between the impulses of the lay public and the actual governing of the economy. This gap between the role of citizens on the one hand and the actual business of economic policymaking on the other must instead be narrowed, allowing citizens to participate not only as bearers of preferences and some local knowledge, but also as sustained and ongoing agents in the task of policymaking.

Regulation and democratic political agency

The need to create spaces for citizens to engage in this experience of policymaking suggests that we look beyond the traditional focal points of democratic theory on elections and legislatures. In fact, much of the actual practice of contemporary governance takes place outside of the electoral-legislative arena, in what we might term "front-line" institutions of governance—regulatory agencies, local-level bodies, and the like. These regulatory institutions are more traditionally seen as merely technical domains of implementing already-settled legislative judgments. But despite the central focus on legislatures, it is in these bodies that the actual practice of devising rules, implementing them, adjudicating disputes, and revising these rules in light of changed conditions takes place.

Contemporary democratic theory either ignores or misunderstands these front-line institutions of regulatory governance. First, many theories of democracy simply ignore or sidestep the domain of regulation and policy implementation. But empirically, there is more to the practice of democracy than electoral and

legislative politics; as such democratic theories that ignore the regulatory state are at best incomplete, and at worst, inconsistent to the degree that the dynamics of regulation undermine values of democratic participation, equality, and contestation. Second, other accounts accept the central role of regulatory institutions as a threat to democracy, but a tragic one, a necessity in a complex modern society where generalist legislatures have no choice but to delegate extensive authority to technical regulatory institutions. On this account, genuine democracy is an ideal of an earlier era, unsuited for the modern world of economic and technological complexity and mass nation-states—a world that demands expert-driven and rationalized policymaking. This turn to bureaucracy may be a progressive modernization of government, or a fatalistic trap of modernity where government must necessarily function in a routinized and bureaucratized manner divorced from ideals of self-government. Finally, a large group of scholars and practitioners see the tension between regulation and democracy as real, but as largely resolved: regulatory agencies are reconciled with the ideals of democracy because they are subjected to oversight be elected officials, procedures that encourage deliberation, opportunities for citizens to provide input, deliberate, or collaborate on agency policies. To the extent that regulatory agencies pose a problem for democracy, then, the root of the problem lies in the "core" domains of democratic politics: background disparities in political organization, or failings in the electoral, representative, or legislative processes.

By contrast, I argue in this project that securing the moral value of democracy as experience requires that we engage more directly with these institutions of regulatory governance—and that these institutions offer an as-yet-unrealized potential as sites for participatory, contestatory democratic politics.

These institutions offer a key arena in which the ideal of democratic political agency can be realized, where the democratic agency of citizens can be fostered, catalyzed, multiplied. Agencies can provide institutional spaces that are a "continuation of the public's and the legislature's broader process of reasoning about what we should do."[25] As institutions tasked with the development and implementation of specific policies, regulatory agencies can serve as a unique "nexus of democracy and governance," creating spaces for citizens to engage directly in policy formulation and implementation in a way that is difficult in context of traditional democratic institutions of elections and legislatures.[26] Regulatory agencies can potentially serve as an enhancer of democratic self-governance, offering a more robust experience of participation, deliberation, and the empowerment of all affected interests.[27] But these regulatory institutions as currently constituted to not yet act as spaces for such democratic participation. To do so, they must be reformed to better facilitate the democratic political agency of citizens themselves. There are four conditions that enable this kind of democratic political agency.

First, the ability of citizens to mobilize and engage in democratic politics depends crucially on having a focal point, or target for such mobilization. Without a sense of where to voice a claim or challenge an action, it is difficult to generate citizen engagement. This suggests that the channels of political authority in

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[25] Henry Richardson, *Democratic Autonomy: Public Reasoning About the Ends of Policy* (New York: Oxford University Press 2002), 13.

[26] See Chris Ansell, *Pragmatist Democracy: Evolutionary Learning as Public Philosophy*, (New York: Oxford University Press, 2011), 3-4.

[27] Mark Warren, "Governance-Driven Democratization," *Critical Policy Studies* 3:1 (April 2009), 3-13.

economic governance must be legible, not hidden away, and consolidated rather than fragmented into a complex and hard-to-navigate ecology of institutions.

Second, these institutions must have sufficiently broad powers to actually respond to the claims made by citizens. This capacity to respond is an important factor in generating meaningful participation; the engagement of citizens depends in part on the likelihood that mobilization will produce a response—and on the presence of an institutional focal point or arena against which mobilization can crystallize, take place, and make claims.

Third, these institutions of governance must be restructured to foster, enable, and facilitate empowered participation by citizens, whether through procedural requirements for participatory policymaking, decentralization, or both. Further, such participation must be meaningful, and take place throughout the life-cycle of policymaking. Rather than simply providing input into a fundamentally elite- or expert-driven policy process, citizens must have the powers to initiate claims, contest decisions, monitor and facilitate implementation, and revise policies in the future.

Fourth, this participatory engagement must be structured to embrace political disagreement and moral judgment. Rather than sterilizing or depoliticizing the issue at hand, democratic institutions must find ways to engage the moral heart of the issues, engage citizens at this level, balance the moral and the technical dimensions of policy debates, and structure citizen engagement so as to cultivate productive contest and moral judgment.

These conditions for democratic political agency can be achieved in front-line institutions of regulation and governance. In contemporary American democracy, these institutions are especially prevalent in two domains: national

regulatory agencies exercising delegated power from Congress on the one hand, and local level governmental bodies created by state charters on the other. Where regulatory agencies offer untapped spaces for democracy that have expansive authority but insufficient channels of participation, local governments tap into a deep tradition of grassroots democratic aspiration, but lack meaningful institutional powers to make this participation effective and meaningful.

Thus, regulatory agencies, normally seen as the bastion of apolitical expertise, can in fact serve as a potentially transformative institutional site for this kind of democratic political agency, if appropriately reformed. These agencies already possess expansive powers to devise, implement, and revise rules. But their authority that is often too fragmented and illegible to the general public, lacking in sufficient channels for meaningful participation, and exercised through an overly apolitical, morally neutral discourse for policy judgments. These features of the regulatory state stem from the traditional view of regulatory bodies as tasked with the mere implementation of already-settled normative policy judgments, located downstream from the more politicized domains of elected branches of the legislature or the executive. Instead, we should reform regulatory agencies sites of democratic participation. Regulatory agencies are exactly the right place for this kind of participation for it is in these front-line institutions that much of the practice of political judgment in modern policymaking takes place. It is in regulatory agencies that general precepts in legislation are clarified, refined, and applied to particular policy contexts—and where these policies are often contested and revised on an ongoing basis. The regulatory state should be reconceived as an expansion of our collective capacities to respond dynamically to a range of modern

harms from the decentralized market to the economic, social and ecological risks of complex technology to newly threatening concentrations of private power.

Similarly, local-level governance institutions like municipal governments offer a unique potential space for fostering democratic political agency. Where national regulatory agencies possess expansive but insufficiently participatory authority, local governments have the inverse problem: valorized as bastions of grassroots participation, but in fact lacking in the capacities to make such participation meaningful. Indeed, while localism has often been a touchstone of democratic theories, it is surprising how little of this aspiration translates into meaningful democratic possibility. On the one hand, the local is treated as a form of market choice: citizens engage with the local as consumers, moving to different localities to fulfill their preferences for space, public goods, and the like. On the other hand, the local can be overly romanticized, as a bounded and intrinsic community, divorced from national and regional concerns. Moreover, in practice, local government institutions are severely hampered in their ability to make public policies. By contrast, the focus on democratic political agency would suggest empowering and restructuring local governments to expand their powers, facilitate participation within them, and integrate local policymaking with national-scale dynamics.

Chapter outline

The following chapters explore these themes, drawing on the intellectual history of debates over economic regulation, contemporary normative theory, and debates in public law. Through these excursions into history and law, the

following chapters attempt to give clarity and concreteness to the abstract aspirations for democratic economic governance. These chapters also make recurring reference to debates over financial regulation as a running example, where these divergent views of laissez-faire, technocratic, and democratic economic governance have been articulated, tested, and given voice through public policy. Much of the debate from 2009-10 for example pitted laissez-faire understandings pushing for deregulation against technocratic vision calling for greater insulated expert oversight. What was often missing in this debate is a version of the more democratic understanding of economic governance, which emphasizes a more substantive vision of economic reordering achieved through participatory mobilization. Indeed, financial regulation also provides an especially difficult case for aspirations to democratic economic governance. Although finance has historically been one of the primary villains for waves of economic reform movements, it is also a domain that seems so overwhelmingly complex and critical that an appeal to markets or experts may be more prudent than to entrust its oversight to lay citizens. If the central challenge for democratic economic governance is to imagine a way for democratic participation to respond effectively to the problems of the market and the regulatory state—when both markets and expertise can lay claim to attractive arguments for their epistemic superiority and robustness to corruption, capture, or inefficiency—this challenge seems especially difficult in context of financial reform.

Part I outlines the dynamics and limitations of laissez-faire and technocratic governance. **Chapter 2** examines the politics and discourse of the financial regulation debate in the Obama era. This exploration highlights the degree to which our current economic policy debates are dominated by a binary clash

between laissez-faire and technocratic visions of economic governance, and the degree to which the long-term aspirations for a more just and democratic economy depend on developing a more robust moral foundation than the kind offered by the technocratic vision. The problem of financial regulation—like other similar policy and institutional reform debates—is thus not just a matter of technical policy design; it is also fundamentally a challenge at the level of ideas, of how we conceive of, understand, and seek to remake our political economic order.

The relative supremacy of this technocratic view of economic governance, however, itself is a product of a long historical trajectory—and represents only one possible tradition of economic reform politics. The origins of our modern discourses and institutions of economic governance can be traced to the rich normative and institutional debates of the Progressive Era from 1880-1920. These reformers took as their central challenge the task of overcoming laissez-faire political thought by building new movements for economic reform and democratic renewal. **Chapter 3** examines the dynamics of laissez-faire thought and the Progressive attack on laissez-faire. In this chapter, I argue that the laissez-faire thinkers of this period espoused the nuanced normative and institutional view of markets as both domains of freedom and as institutions that, unlike state actors, possessed a superior robustness to capture and corruption: while legislatures could be co-opted by special interests, diffuse markets could not. Progressive Era critics exploded this laissez-faire view through a powerful critique of the market as a system of power, coercion, and pervasive social harm. The challenge for these reformers was to find a way to respond to the dangers of the new market economy through political institutions that were nevertheless robust to the kind of capture and corruption that laissez-faire thought warned against. The result of this

ferment was to seed multiple traditions of economic reform: not only through the creation of new expert-led regulatory bodies, but also through the democratic appeal to the power of the people to hold both markets and states accountable to the public good.

Of these two Progressive traditions, it is the technocratic one that came to prominence over the rest of the twentieth century. **Chapter 4** traces the rise, critique, and fall of this technocratic approach to economic governance. At its height in the New Deal, this technocratic aspiration sought to make good on Progressive critiques of the market, resolving market instabilities while avoiding the same concerns of political corruption and chaotic democratic politics through the deployment of rational, scientific expertise. But as faith in this expertise waned in the later twentieth century, the regulatory state underwent waves of reform through shifting currents in modern administrative law, each of which struggled to preserve the effectiveness and immunity to corruption of technocratic regulation. The image of technocratic governance as rational and effective proved an illusion, succumbing to the resurgence of laissez-faire critiques during the late twentieth century.

The rise and fall of the technocratic vision as a way of responding to the dangers of the market economy creates the dilemma faced by contemporary reformers in economic governance debates. The dislocations and threats of market society remain matters of central public concern, but the preferred mode of response—the appeal to insulated expert regulation—no longer commands the faith as it did at the height of the New Deal, subject instead to a pervasive anxiety about the corruption and capture of regulatory authority. If the solution to the problems of the market is a turn to technocratic governance, but such technocratic

institutions are themselves seen as reservoirs of unaccountable or captured authority, then this places contemporary critics of the market in a difficult position. Yet as the brief historical account in Part I suggests, this technocratic vision is only one possible manifestation of the myriad of ideas generated out of the Progressive critique of the market. Many of these critics turned not just to expertise but also to the renewed political power of citizens themselves as a way to address the dangers of the market while also avoiding the risks of special interest influence and capture. **Part II** turns to these alternative threads to develop an account of democratic economic governance.

In **Chapter 5**, I argue that the central motivating concern in economic governance is one of agency. Economic policy issues are not simply matters of inefficiency or market failure. The modern market economy is morally troubling not just because of its distributional consequences, but because it creates powerful private actors such as firms and diffuse systemic market forces that seem to defy our ability as citizens to contest, challenge, and revise. The problem of the economy is fundamentally, then, a problem of political agency. This argument suggests that in order to respond to the threats of the market economy in a manner consistent with democratic ideals, we need an institutional structure for regulation that expresses and facilitates, rather than limits, the political agency of citizens themselves to engage in self-government. The most compelling moral defense of the modern regulatory state is that it expresses our collective will as democratic citizens in responding to these threats of private and market power.

But as **Chapter 6** suggests, this claimed link between democratic citizens and the regulatory state is more of an illusion than a reality. Contemporary administrative law claims to have reconciled the tension between democracy and

regulation, casting the regulatory state as precisely such an expression of the collective democratic will. But the most prominent attempts to theorize this link between democratic agency and the regulatory state ultimately position citizen action at too far a remove from the actual exercise of regulatory authority. In practice, administrative law thus papers over rather than actually resolves this fundamental tension between a commitment to democratic self-rule on the one hand, and the use of regulatory agencies to address problems of a complex market economy on the other. These debates in contemporary administrative law do, however, suggest elements of a more democratic regulatory state, particularly pointing to the need to rethink regulation along more participatory and contestatory lines.

Chapter 7 then develops the conceptual foundations for a more democratic approach to economic governance. In contrast to the technocratic appeal to expert-derived economic regulations developed through insulated institutions that bear the sanction—but not the participation—of citizens, this chapter argues that we ought to adopt a different understanding of both the concept of democracy and the concept of regulation. I argue here that democracy should be understood as fundamentally a matter of experience in the practice of self-government. This view suggests that to achieve democracy as experience, we need institutions that do more than simply consult with or gather the input of citizens. Rather, we need institutions that can place citizens in situations where they are engaged in the actual challenges of making judgments, implementing policies, learning from the repercussions of their decisions, and then revisiting those judgments iteratively over time. This view of democracy in turn suggests that regulation be understood not as the technical implementation of already-determined political judgments, but

rather as the domain where this kind of actual governing takes place—where general principles are translated into policies in particular circumstances. Drawing on the thought of some of the more radical Progressive Era democratic thinkers like John Dewey and Louis Brandeis, this chapter then develops principles with which we can guide the reform of regulatory institutions to function as such sites of democratic experience. In particular, this chapter suggests that these institutions must: first be organized to provide focal points as targets for citizen mobilization; second, possess the authority to respond to these claims; third, empower citizens to engage in governing decisions alongside experts; and fourth, allow these judgments to take place through moral, and not merely technical, discourses and debates.

With this conceptual framework in hand, the book returns in **Part III** to the kinds of concrete institutional and policy questions that began the inquiry to trace what this democratic alternative might look like, using the debates around financial reform as an ongoing example. **Chapter 8** examines how this democratic approach would require a more participatory structure to the modern regulatory state, as a space in which citizens could experience the challenges of governance, and through which these more moralized debates can be productively channeled. Again, the recent politics of financial reform provide an illustrative example of how this democratic approach would suggest a different institutional reform agenda than the one pursued. **Chapter 9** provides a parallel argument in context of local government reforms, suggesting how these institutions can be made more effective democratic forums, and using the debates over financial reform and predatory lending as an example.

Chapter 10 develops the theme of moral judgment in economic policymaking. This chapter argues that, despite the efforts of technocratic thinkers

to cast economic policy as a matter of neutral expertise, economic judgments are inextricably moral judgments, and thus ought to be engaged as political decisions through a process that better integrates citizens and experts. Using the examples of attempts to address the problems of TBTF firms and speculative derivatives, this chapter shows that viewing these issues in a narrow technical register actually gives rise to pathological and overly formalistic policy approaches. By contrast, a repoliticization of these debates as moral and political judgments unlocks a broader institutional palette of potential responses. This impulse towards moral avoidance also helps explain the drive away from the kind of democratic institutions explored in Chapters 8 and 9. Technocratic governance depoliticizes these issues and delegates them to expert-led institutions. Repoliticizing these policy debates must come with a similar shift to more democratic institutions for deciding these issues.

PART I

2 EXPERTISE AND DEMOCRACY IN FINANCIAL REFORM

After the immediate urgency of the 2008-9 financial collapse began to fade, the policy conversation shifted to the longer-term question of how to reform the financial system to prevent such catastrophic crises from recurring. Much of the debate revolved around technical matters such as incentives for financial firm executives to prevent excessive risk-taking; improvements to regulatory models of financial markets; capital requirements for banks and risk-mitigating regulations on complex securities trading.[1] The debate also generated widespread interest and mobilization, not only by financial sector firms trying to stave off new regulations, but also by citizens' groups advocating in favor of even more aggressive proposals. The battle for financial reform pitted proponents of expanded oversight in the Obama administration against conservative critics of regulation. But it also highlighted a tension among reformers themselves: between those in the administration calling for an expansion of expert regulatory oversight, and a number of dissident voices proposing more radical and structural constraints on the powers and size of financial firms themselves. The financial reform debate became a key battleground for and window into deeper debates over the future of American democracy and economy. What role should finance play in sustaining a productive economy? How could financial firms be regulated effectively: through

[1] See e.g. Joseph Stiglitz, "The Financial Crisis of 2007-8 and Its Macroeconomic Consequences," in Stephany Griffith-Jones, Jose Antonio Ocampo, and Joseph E Stiglitz, eds., *Time for a Visible Hand: Lessons from the 2008 World Financial Crisis* (New York: Oxford University Press 2010), 19-41.

market incentives, or through expert regulatory oversight, or through more structural constraints on financial firms?

In the end, it was the technocratic view of financial regulation as problem of expert macroeconomic management that carried the day. As a result, the primary change in the post-crisis system of finance has not been in the structure and dynamics of industry itself, but rather in the mode of oversight. Dodd-Frank focuses much of its attention on expanding the authority, resources, and coordination of technocratic financial regulatory agencies. The underlying theory of reform animating the bill is that the problem of financial regulation is best resolved by appeal to neutral, insulated, expert regulators who are given sufficient authority, resources, and coordination to effectively manage the modern financial system.[2] But this legislation has not resolved the debate over how to handle "too-big-to-fail" (TBTF) financial firms. Over four years after the crisis, analysts are already warning of the threat of a repeated financial collapse and the persisting "systemic risk" posed by "too-big-to-fail" financial institutions, while anxieties persist about the efficacy of regulatory agencies themselves.

This chapter explores the discourse of the financial reform debate to show how this technocratic response to the problem of TBTF firms emerged out of a discursive framing of the problem of financial regulation in distinctly technocratic terms. For most mainstream reformers, the very problem of financial reform was intrinsically a matter of expert management to resolve market failures, excessive risk, and to protect consumer welfare. More radical proposals of structural limits

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[2] See generally, K. Sabeel Rahman, "Envisioning the Regulatory State: Technocracy, Democracy, and Institutional Experimentation in the 2010 Financial Reform and Oil Spill Statues," *Harvard Journal on Legislation* 48 (2011), 555-590.

on TBTF firms, by contrast, were couched in a different discourse that emphasized not the role of expert management of technical matters like systemic risk, but rather more democratic concerns of holding the power of private firms to account. This contrast—and the relative dominance of the technocratic vision—captures neatly the broader problem of how our contemporary views of economic governance are overly oriented around the technocratic, to the marginalization of the democratic.

Financial reform as risk management and consumer protection

In hindsight, the 2008 crisis itself was caused by the rise of new financial activities that magnified economic risks outside the purview of the regulatory architecture inherited from the New Deal era and altered significantly during the deregulatory turn in the 1980s and 1990s. During the 2000s, subprime mortgage lending—the offering of mortgages to borrowers to would not traditionally qualify as safe loans—increased dramatically. So too did the increase in complex new financial securities such as credit default swaps and collateralized debt obligations. These securities packaged and repackaged mortgage loans into new assets that were then sold, repackaged, and sold again. Securities dealers argued that this effectively distributed the risk of potential declines in the value of subprime mortgages, while offering safe assets for a wide range of investors including pension funds and money market mutual funds. But when the value of subprime mortgages started to decline, the diffusion of mortgage-backed securities helped provoke a vicious cycle of liquidation, as investors panicked and sought to sell their securities. The result was a classic run, only this time it was a run not on

bank deposits as in 1929, but rather on short term financial securities such as the repo agreements and money market mutual funds—financial products which were tainted by mortgage-backed securities, but had come to function like money for many businesses. As a result, when Lehman Brothers collapsed, credit effectively froze, bringing the broader economy to a halt. Companies that have come to rely on these short-term credit lines could no longer make payroll or pay for investments, leading to spillover effects on the broader economy.[3]

The discourse of the financial reform debate is indicative of how reform efforts interpreted and responded to these events through a predominantly technical and technocratic understanding of the core problems. The debate over financial reform and the problem of TBTF firms played out through a number of competing narratives each of which sought to frame the problem of the crisis, and suggest a set of policy responses. Such public narratives play a major role in diagnosing and constructing policy problems, reworking moral and institutional understandings, and ultimately in shaping policy responses.[4] The mainstream discourse of financial reform revolved primarily around two narratives in particular: first, a narrative of risk management; and second, one of consumer

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[3] See generally, The Financial Crisis Inquiry Commission, *Financial Crisis Inquiry Report* (New York: Public Affairs, 2011); Morgan Ricks, "Regulating Money Creation After the Crisis," *Harvard Business Law Review* 1 (2011), 75-143.

[4] On how political narratives shape the terrain of political possibilities for reform, see Daniel Carpenter and Gisela Sin, "Policy Tragedy and the Emergence of Regulation: The Food, Drug, and Cosmetic Act of 1938," *Studies in American Political Development* 21 (2007), 149-180 (describing one case study of the links between narrative, normative argument, and political mobilization). More generally, political theorists have noted that for political engagement to take place, "what is needed is some articulation of the general threat or, more precisely, an account of the phenomenon and a ground on which it can be seen as politically salient." Mika LaVaque-Manty, *Arguments With Fists: Political Agency and Justification in Liberal Theory* (New York: Routledge, 2002), 18 ("Who says what is . . . always tells a story, and in this story the particular facts lose their contingency and acquire some humanly comprehensible meaning"). Hannah Arendt, "Truth and Politics," in Jerome Kohn, ed., *Between Past and Future: Eight Exercises in Political Thought* (New York: Penguin Books, 2006), 223-260, at 257.

protection. But while these narratives did help animate, justify, and promote what became the Dodd-Frank reform statute, they created a dominant understanding of the financial crisis as primarily a problem of market failure, calling for the solution of technocratic management. In so doing, these dominant reform narratives not only grounded the technocratic ethos of Dodd-Frank; they also sterilized the problem of the financial crisis itself of much of its more charged moral dimension. Rather than being a matter of the concentrated economic and political power of the financial sector, or of a proliferation of socially undesirable "speculation," the issues were constructed and understood through apolitical technical terms of stability and consumer protection.

These policy narratives had to navigate three core tensions. First, they each sought to promote expanded financial regulation while overcoming deep-seated and resilient prior commitments to self-correcting, efficient, and socially optimal markets. Since the 1980s, political and intellectual currents underscored the return of this view that free markets are the optimal mode of organizing social behavior, and that any attempts to regulate or alter the workings of the market are likely to fail, causing even worse results or jeopardizing underlying moral values such as individual liberty.[5] Second, they each had to overcome an ambiguity and anxiety about who the real villains in the financial crisis were: big private corporations like Wall Street firms, or "big government," who had come to the aid of Wall Street through the unpopular TARP bailout program in 2008-9. While these bailouts were widely credited with averting a more catastrophic economic collapse, they

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[5] See Margaret Somers and Fred Block, "From Poverty to Perversity: Ideas, Markets, and Institutions over 200 Years of Welfare Debate," *American Sociological Review* 70:2 (2005), 260-87. On the revival of free-market ideology in the 1980s and 1990s, see Daniel Rodgers, *Age of Fracture* (Princeton: Princeton University Press, 2010), 41-76.

revived anxieties about state intervention and raised the specter of government capture by the financial industry—thus partly counteracting the degree to which the crisis itself cast doubt on free-market ideology itself. Finally, these reform discourses had to overcome the complexity of financial stability policy. Most policymakers were in the dark about the dizzying array of financial securities and practices that ultimately gave rise to the crisis. This complexity made the crisis difficult to understand, and thus difficult to distill into a narrative of cause, effect, and response. Indeed, the more complex a social challenge, the more likely it is to be seen by actors as beyond the scope of political action, more akin to forces of nature or accident.[6]

The first central narrative employed in the financial reform debate was one of *risk management* to ensure market stability. In this narrative, the problem of the financial crisis was one of excess risk-taking. The solution, therefore, was to improve federal regulatory oversight from agencies like the Federal Reserve or the Securities and Exchange Commission to prevent excess risk-taking by financial firms, thereby ensuring the long-term stability of the free market. In his signature speech defending and outlining the financial reform push, President Obama emphasized how these regulatory reforms would make financial markets work better by alleviating the risk of systemic collapse:

> The problem is that these [financial] markets operated in the shadows of our economy, invisible to regulators, invisible to the public. So reckless practices were rampant. Risks accrued until they threatened our entire financial system. … these reforms are designed to respect legitimate activities but prevent reckless risk taking.[7]

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[6] Deborah Stone, "Causal Stories and the Formation of Policy Agendas," *Political Science Quarterly*, 104:2 (1989), 281-300, at 288-9.

[7] Barack Obama, speech on financial regulation, Cooper Union, New York, April 22, 2010.

The language of risk can be a powerful one, "pushing a problem out of the realm of accident into the realm of purpose"—in this case making the financial crash a phenomenon capable of amelioration through reform.[8] Indeed, the idea of government as risk-manager animates many of the major elements of the modern regulatory and welfare state, from Social Security to unemployment insurance.[9] From a policy standpoint, efforts to mitigate excessive risk-taking for example by expanding capital requirements for financial firms may be prudent. But the narrative of risk leaves out as much as it enables. What is notably missing from this account is any sense of moral blame for those who caused the crisis in the first place, any appreciation for the role that economic and political power plays in creating situations of social risk in the first place—and distributing that risk in unfair and unequal ways across different social classes. This narrative also tellingly privileges financial regulatory experts as the primary responders. It makes the problem of finance a technical one of market failure and misaligned incentives to be optimized by expert oversight and management. There seems to be little role for citizens or social movements except as passive victims of risk or beneficiaries of elite risk management. While this language is well-suited for justifying and shaping particular policy changes, by itself it provides little by way of deeper diagnosis, moral critique, or articulation of a cohesive identity for reformers—elements that undermine the impact of this kind of narrative for a broader social movement.

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[8] Stone, "Causal Stories," 290.

[9] David Moss, When All Else Fails: Government as the Ultimate Risk Manager (Cambridge: Harvard University Press, 2002).

The second competing master narrative of the financial crisis focused not on macroeconomic risk, but on the needs of consumers themselves by emphasizing the goal of *consumer protection*. In this narrative, advocates of reform argued that consumers needed greater regulatory protections from unfair or misleading financial products such as excess credit card fees and predatory adjustable-rate mortgages. Again, this narrative provided an account of the crisis—that it partly stemmed from unfair lending practices that put consumers deeper in debt—that justified a particular reform, the creation of a Consumer Financial Protection Bureau (CFPB). And like risk-management, the discourse of consumer protection has helped motivate many valuable policy reforms. The creation of the CFPB, in particular, represents a major achievement, establishing for the first time a regulatory body dedicated to protecting the interests of consumers across the universe of financial products from credit card and home mortgage terms to student loans.

The language of consumer protection is one step better than that of risk management insofar as it does channel some moral considerations in its emphasis on fairness, its critique of manipulation or excessively harsh lending terms, and in its background ideal of equal access to financial products. But consumer protection is at best only a half solution, for while it can offer a defense of individual consumer interests against the interests of the financial industry, it is difficult to fully motivate broader changes to the nature of modern finance itself as a response to the problem of consumer protection. As historian Lizabeth Cohen argues, the consumer rights discourse, while at times becoming a way of "mitigating the excessive power or other political blocs" by empowering consumers as a "residual

category" or interests capable of "speaking for the public,"[10] it can also fade into a more subdued push to protect the interests of consumers as purchasers of goods in a market society.[11] Indeed, while individual policies to ensure fair and transparent financial products are beneficial, it remains to be seen whether such pro-consumer efforts will fundamentally alter the power relationship between finance and citizens, or whether it will result in a more modest change in the polish of existing financial transactions and activities.

This tension inherent in the discourse of consumerism is exemplified by the trajectory of former Harvard Law Professor and later-Senator Elizabeth Warren, who emerged as the creator and primary champion of the CFPB. On the one hand, Warren's advocacy generated widespread grassroots support among reformers, and intense opposition from industry groups and conservatives. But on the other hand, taken at its word the language of consumerism used by Warren herself—and adopted by President Obama—continued to rest on a sense that the goal of reform was not to fundamentally alter the dynamics of modern finance but rather to simply ensure that markets worked more efficiently by curtailing unfair or deceptive practices. As Obama argued, "with a dedicated agency setting ground rules and looking out for ordinary people in our financial system, we will empower consumers with clear and concise information when they're making financial decisions," thereby creating an economy that "works for all of us."[12] Warren similarly argued in her original piece proposing a CFPB that such a regulatory

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[10] Lizabeth Cohen, A Consumer's Republic: The Politics of Mass Consumption in Postwar America (New York: Knopf, 2003), 24.

[11] Cohen, A Consumer's Republic, 345-97.

[12] Obama, speech at Cooper Union, April 22, 2010.

body would protect consumers from unfair terms in credit cards, auto loans, and mortgages, ensuring "minimum safety standards" for these financial products.[13] It is telling that Warren's greatest political impact lay not in this appeal to 'making markets work better' but rather in her *symbolic* role as a representative for the interests and aspirations of ordinary citizens as against the financial industry. Put another way, despite the language of optimizing market functioning, Warren's moral appeal and political force came not from her claim to market optimizing or technical expertise, though she possessed plenty of that as well; rather it stemmed from an entirely different source: her position as an advocate and defender of the decidedly moral and political interests of ordinary families. The real value of the consumer protection narrative, then, is not in its defense of the wants of the consumer, but rather insofar as it channels more fundamental moral concerns into the vessel of consumer protection: a concern with financial sector power; a sense of outrage at the unfairness imposed upon ordinary citizens; and the sense that citizens need an organized and institutionalized source of countervailing power to provide a check on and accountability for industry.

Both narratives of risk management and consumerism were common between 'insider' leaders like President Obama and Congressional advocates for reform, as well as outside experts like Warren. These narratives were also supported and employed by outside lobbying groups that aimed to mobilize public support for the reforms proposed by the administration. Tellingly, the main

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[13] Elizabeth Warren, "Unsafe at Any Rate," *Democracy Journal* (2007), 8-19, at 18.

umbrella organization for these outside groups, Americans for Financial Reform, took their rhetorical and policy cues from Warren and Obama.[14]

These conceptual frameworks in turn gave rise to the reform proposals that would eventually take shape in Dodd-Frank. The Obama administration's white paper released by the Treasury in spring 2009 is indicative. A key agenda-setting document that formed the starting point for the drafting of Dodd-Frank, the white paper cast the problem of financial regulation as being fundamentally one of managing risk and promoting consumer protection. The problem was fundamentally a decline of regulatory oversight: "gaps and weaknesses in the supervision and regulation of financial firms presented challenges to our government's ability to monitor, prevent, or address risks before the built up in the system."[15] The response, then, required a renewal of regulatory capacity such that expert regulators could engage in better oversight. Crucially, the white paper emphasized the importance of restoring oversight without undermining the basic structure of the financial sector, and the innovation that it contributed to economic growth and well-being.[16]

Similarly, the Congressional Oversight Panel led by Elizabeth Warren charged with investigating the financial crisis in advance of the legislative policy debate in Congress offered much compelling rhetoric, but a more tentative reform package. The report, for example, opens with a frank acknowledgement that finance was an "inherently volatile" industry, in need of strong governmental

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[14] See Americans for Financial Reform, http://ourfinancialsecurity.org/

[15] "Financial Regulatory Reform: A New Foundation: Rebuilding Financial Supervision and Regulation," Department of the Treasury (Spring 2009), 1.

[16] *Ibid*.

regulation to ensure that the financial system serves its core "public function" of channeling savings into investment.[17] The report directly attacked the failed "regulatory philosophy" of free market deregulation, instead emphasizing the value of regulation as a way of promoting the democratic public good—which should be understood not in terms of economic output but rather in terms of the "flourishing" and "quality of life" enjoyed by ordinary citizens.[18] Yet here too, the actual recommendations of the report revolved around the model of expert-based regulations focused on the more narrow task of closing market failures, promoting transparency, and establishing consumer protections.[19]

The limits of expert management

These discursive understandings laid the foundation for the drafting and passage of Dodd-Frank. While the final bill took a more moralized approach on certain issues like mortgage lending, where reforms called for more strict requirements aimed at protecting homeowners against the malfeasance of lenders,[20] when it came to the central issue of regulating TBTF firms and addressing issues of financial stability, the overall response of the statute was to take a more technocratic approach, emphasizing expert oversight as the key to closing market failures and making the financial system safer and more efficient.[21]

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[17] Congressional Oversight Panel, *Special Report on Regulatory Reform* (January 2009), 2-3.

[18] Congressional Oversight Panel, *Special Report*, 19-20.

[19] See Congressional Oversight Panel, *Special Report*, 4.

[20] See Dodd-Frank Act, tit. XIV.

[21] See generally, Rahman, "Envisioning the Regulatory State".

Dodd-Frank itself focuses primarily on efforts to expand the authority, coordination, and resources of financial regulatory agencies to prevent regulatory gaps over the 'shadow banking sector' and to enable oversight of risky financial products like derivatives. Crucially, the specific content of these regulations is left largely to the discretion of the regulators themselves. For example, the centerpiece of Dodd-Frank's financial stability policy is the creation of a Financial Stability Oversight Council (FSOC), comprised of the heads of all the major financial regulatory agencies such as the Securities and Exchange Commission (SEC), the Commodity Futures Trading Commission (CFTC), and Office of the Comptroller of the Currency (OCC), housed in the Fed, and charged with the task of coordinating among the agencies and developing regulations to identify systemic risks to the financial sector and tailor appropriate regulatory responses. The FSOC has wide discretion; many of the more specific reform proposals on financial stability—such as the proposed 15-to-1 leverage cap on financial firms, or the option to break up systemically risky TBTF entities were codified not as statutory directives, but rather as options to be implemented as needed at the discretion of the FSOC itself. In a similar spirit, other provisions in Dodd-Frank provide greater authorities to financial regulatory agencies like the SEC and CFTC, for example, empowering them to regulate derivatives,[22] credit rating agencies,[23] and municipal securities,[24] and hedge fund advisors.[25]

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[22] Dodd-Frank Act tit. VII.

[23] Dodd-Frank Act tit. IX, subtit. C.

[24] Dodd-Frank Act tit. IX, subtit. H.

[25] Dodd-Frank Act tit. IV; *e.g.*, § 402(a) (amending 15 U.S.C. § 80b–2(a)) (extending CFTC authority to private funds under the Investment Advisors Act of 1940, 15 U.S.C. 80b-2(a)); § 403 (amending 15 U.S.C. § 80b–3(b)) (eliminating the private fund exception to CFTC authority).

In addition to these grants of broad regulatory authority to federal agencies, it is striking how Dodd-Frank attempts to rationalize—and legitimate—such expanded regulatory authority. First, several provisions of the act explicitly attempt to promote the rationality and effectiveness of regulation through greater coordination between agencies,[26] especially by the FSOC.[27] Second, while it grants agencies broad discretion in setting specific regulatory policies, the statute also requires these decisions be backed by greater expertise and research, whether through research studies[28] particularly through the newly established Office of Financial Research,[29] agency-created technical advisory boards,[30] or data collection.[31] Third, where the legislation provides for external checks on agency regulations, these checks seem built primarily to ensure the rationality and expertise of agency actions through statutory requirements for cost-benefit analysis,[32] congressional audits of agencies,[33] and the use of agency inspectors

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[26] Dodd-Frank Act tit. VII, subtit. A (Empowering the FSOC and judicial review to coordinate and arbitrate disputes between the SEC and CFTC which are granted shared authority over derivatives markets).

[27] Dodd-Frank Act § 119 (to be codified at 12 U.S.C. § 5329).

[28] *See, e.g.*, Dodd-Frank Act tits. I–II (requiring FSOC studies on systemic risk); tit. V (requiring Federal Insurance Office to study and monitor the insurance industry to advise the FSOC); § 1013 (to be codified at 12 U.S.C. § 5493) (creating a dedicated research arm for the CFPB to investigate consumer financial products and develop regulatory options); § 417 (SEC studies on short-selling); § 914 (amending 15 U.S.C. § 80b-11) (possible investor advisor certification requirements); § 917 (improvements to investor financial literacy); § 918 (improvements to mutual fund advertising); §§ 1074, 1077 (requiring studies of the desirability of further regulation in areas such as mortgages and private education loans).

[29] Dodd-Frank Act tit. I, subtit. B.

[30] Dodd-Frank Act § 111(d) (to be codified at 12 U.S.C. § 5321).

[31] Dodd-Frank Act § 112(d)(3) (to be codified at 12 U.S.C. § 5322).

[32] Dodd-Frank Act § 1022 (to be codified at 12 U.S.C. § 5512).

[33] Dodd-Frank Act §§ 962-964 (amending 15 U.S.C. §§ 78d-7 to 78d-9).

general.[34] Finally, the statute includes several provisions to improve agency expertise, neutrality, and autonomy, for example requiring a study to improve the SEC's the agency's autonomy and effectiveness at enforcement,[35] and to reform revolving-door policies to limit lobbyist influence.[36]

Many of these provisions of can be traced to difficulties in the negotiations over the reform bill in Congress, and to a political environment that in many ways was hostile to more far-reaching reform. The sheer multiplicity of regulatory agencies at the federal and state level has created a problematic politics of turf battles between agencies, creating inefficiencies and regulatory loopholes as agencies themselves attempt to undermine the authority and capacity of rivals.[37] Similarly, gridlock in Congress may have produced more inefficiencies in the statute itself, particularly as more innovative reform ideas were rejected as they came from those who lacked influence in Congress.[38] Although the reform debate did draw in a broader set of policymaking experts and academics, the financial reform debate largely left out unions, activists, and thinkers outside of the finance policy domain.[39] The disparity in political power between the financial industry, and other more grassroots organizations representing workers and other citizens

[34] Dodd-Frank Act § 211 (to be codified at 12 U.S.C. § 5391).

[35] Dodd-Frank Act § 967.

[36] Dodd-Frank Act § 968.

[37] Daniel Carpenter, "Institutional Strangulation: Bureaucratic Politics and Financial Reform in the Obama Administration," *Perspectives on Politics* 8:3 (2010), 825-46, at 832-7.

[38] Carpenter, "Institutional Strangulation," 826-31 (noting the difficulties faced by reformers like Brooksley Born, Elizabeth Warren, and academics trying to push more aggressive reforms in an area usually dominated by male finance-sector personnel).

[39] Daniel Carpenter, "The Contest of Lobbies and Disciplines: Financial Politics and Regulatory Reform in the Obama Administration," Working Paper, Obama's Agenda and the Dynamics of US Politics (Russell Sage Foundation, 2010).

help skewed not only the legislative result but also the ongoing implementation of reforms through agency rulemakings.

It is telling that the most broadly acceptable policy response to the problem of TBTF firms took the form of this technocratic view of regulation. This framework seeks to expand both the authority and the discretion of agencies to address complex social problems—here, financial crises. This expanded authority is legitimated and constrained, not by statutory directive or other forms of political constraint, but rather through a variety of mechanisms aimed at ensuring that agency actions are expert-driven and rational. Thus, provisions that require agency coordination, research, and cost-benefit analysis temper the specter of relatively unaccountable regulatory authority by rationalizing regulatory governance. Similarly, efforts to improve agency organization and promote autonomy from regulated industry aim towards the same goal of rationalizing agency authority.

This technocratic approach to economic regulation seems to offer a way to pursue the public interest and ensure adaptable and responsive policymaking in a complex modern economy, free of the conflicts, gridlock, or ignorance of raw political disagreement. But the effectiveness and legitimacy of this vision of regulation ultimately rests on the faith that citizens have in the regulators themselves. Insulation and expertise are compelling sources of regulatory legitimacy and effectiveness, but there are reasons to doubt that this technocratic vision is a desirable one. First, there is the concern that the regulators upon whom so much depends may not themselves act for the public good, lacking in sufficient institutional modes of democratic accountability and responsiveness. Second, there is a more subtle concern that in constructing the problem of financial regulation as a technocratic one, this understanding of the problem changes the menu of

substantive policy approaches that may be considered, taking more moralized and perhaps more desirable approaches to financial regulation off the table out of a preference for more neutral managerial approaches.

The first concern of regulatory accountability and disparities in interest group influence and political power is especially clear in the financial reform context. Arguably, agencies like the SEC and the Fed already possessed sufficient tools to prevent many of the risky lending, leverage, and securitization practices that proliferated on Wall Street in the buildup to the crisis, but chose not to do so on the view that most firms knew what they were doing, were already subject to sufficient market and regulatory checks, and were generating good value for the broader economy. Yet many of the substantive policy changes envisioned by Dodd-Frank depend on the discretion and further deliberation of these same regulators who were criticized for failing to hold the financial sector in check during the 1990s and 2000s.[40] This regulatory discretion also provides an opportunity that industry players can exploit to win more favorable policies—a fact underscored by how quickly industry firms mobilized their lobbying efforts to target regulators as soon as Dodd-Frank was passed.[41] This concern is the familiar one of regulatory capture and industry influence, and has been a long-standing challenge for any regulatory reform effort.[42]

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[40] See e.g. Jeff Madrick, "Wall Street Leviathan," *New York Review of Books*, April 7, 2011.

[41] See e.g. Binyamin Appelbaum, "On Finance Bill, Lobbying Shifts to Regulators," *New York Times*, June 26, 2010.

[42] For a good account of the history and policy implications of such regulatory capture debates, see e.g. Stephen Croley, *Regulation and the Public Interest: The Possibility of Good Regulatory Government* (Princeton: Princeton University Press, 2008); Dan Carpenter and David Moss, eds., *Preventing Capture: Special Interest Influence and How to Limit It* (New York: Cambridge University Press, forthcoming, 2013).

The greater the reliance on expert discretion and insulation, the greater the concerns that these experts may use their authority not for the general public good, but rather for the particular benefit of the financial sector itself. Whether as a result of direct lobbying or corruption, or through more subtle forms of cultural and ideological influence where industry interests are shared by like-minded regulators,[43] or the sheer dependency of regulators on industry for information and data,[44] the problem of regulatory capture is especially acute in financial regulation. Even in the early stages of implementing Dodd-Frank, agencies have been heavily lobbied[45] by industry firms and supporting associations like the American Bankers' Association, which have collectively been more aggressive in seeking and winning meetings with regulatory agency officials during the implementation and drafting of these rules, in comparison to consumer advocates or other proponents of tougher regulations.[46] These efforts have weakened proposed regulations, whether by introducing more exceptions and loopholes in the case of new commodity derivatives rules, FSOC rules for systemically-risky institutions,[47] or relatively lax

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[43] For a good overview of different kinds of direct and indirect, cultural, or ideological capture, see Moss and Carpenter, eds., *Preventing Capture.*

[44] This risk of "epistemic capture" is a danger noted by a range of advocacy groups active in financial reform. Industry lobbyists have already hired scores of staff to develop reports and data that can justify regulatory decisions more favorable to industry, leaving countervailing advocacy groups, like the AARP, scrambling to keep up. See, e.g., Binyamin Appelbaum, "On Finance Bill, Lobbying Shifts to Regulations," *New York Times,* June 27, 2010.

[45] Ben Protess, "Wall Street Lobbies Treasury on Dodd-Frank," Dealbook, *New York Times*, April 5, 2011 (describing the disparity in lobbying presence between financial firms and largely absent consumer advocates or other proponents of financial regulation).

[46] Protess, "Wall Street Lobbies Treasury on Dodd-Frank."

[47] Marian Wang, "Regulators Weaken Dodd-Frank Draft Regs, Allow More Risk," *ProPublica*, September 22, 2011; Simon Johnson, "The Financial Stability Oversight Council Defers to Big Banks," Economix Blog, *New York Times*, January 20, 2011 (recounting how early FSOC policy reports are deferring to financial industry interests in defining the costs and benefits of limiting the size of big banks as required by § 123 of the legislation, in some cases ignoring data suggesting the need for more aggressive caps on bank size).

enforcement by the SEC in settling suits against financial firms accused of fraud, rather than exercising the full range of its prosecutorial powers,[48] and declining to enforce the ratings agency rules in Dodd-Frank.[49]

This danger that supposedly insulated, expert regulators will water down regulation in response to industry pressure is particularly well-illustrated by the debate over the Volcker rule. Named after the former Fed chairman Paul Volcker, the Volcker rule contemplates a ban on proprietary trading, where financial firms use their own funds to engage in risky trading. The original Volcker Rule consisted of two parts: an absolute size limitation on financial firms to less than ten percent of market share in loans or deposits, plus a ban on proprietary trading that supporters saw as a way to reformulate and modernize the New Deal era Glass-Steagall provision separating commercial and investment banking.[50] Initially proposed as a bright-line ban, the Volcker rule was notably absent from Treasury's initial white paper setting the terms of Congressional debate. Amendments to Dodd-Frank which sought explicit versions of the Volcker rule, or strict size and activity limits on large financial firms were easily defeated.[51] Indeed, as the Federal Reserve has developed the draft of the Volcker rule, financial sector firms have lobbied successfully to add more exceptions, complexity, and vagueness to the draft rule, on the grounds of needing to protect various market-making

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[48] Shashien Nasripour, "SEC Takes Light-Touch Approach Against Lawbreakers, Critics Say," *Huffington Post*, April 7, 2011.

[49] Gretchen Morgenson, "Hey, SEC, That Escape Hatch is Still Open," *New York Times*, March 5, 2011.

[50] Jonathan Macey, James Holdcroft, Jr., "Failure Is an Option: An Ersatz-Antitrust Approach to Financial Regulation," *Yale Law Journal* 120 (2011), 1368-1418, at 1397.

[51] John Cassidy, "The Volcker Rule," *The New Yorker*, July 26, 2010.

businesses.[52] In the process, the force of the rule is being undermined.[53] As two critics of the Volcker rule noted later, in practice the rule "poses little meaningful limitation on the riskiness of big banks or their interconnectedness or systemic importance."[54]

On one level, this dilution of the rule stems from difficulties in the issue itself: regulators have struggled to identify at a fine-grain level how to really distinguish acceptable from unacceptable forms of trading. Even determining the ten percent concentration level is a complex task, requiring significant discretion and interpretation on the part of regulators.[55] But the substantive challenge of determining what kinds of financial activity to bar is magnified by a procedural disparity in the influence and participation of industry as compared to other countervailing advocacy groups. On the Volcker Rule, the Fed meeting routinely with the top banks like JP Morgan, Bank of America, and Goldman Sachs, but only meeting thrice with consumer advocacy groups like Americans for Financial Reform.[56] A satellite group of the Occupy Wall Street protestors called Occupy SEC combined the work of lay citizen protestors with professionals and academics who had in-depth experience in finance to submit its own 325-page point-by-point

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[52] Jesse Eisinger, "The Volcker Rule, Made Bloated and Weak", Dealbook, *New York Times*, February 22, 2012.

[53] Floyd Norris, "Bank Rules That Serve Two Masters," *New York Times*, October 13, 2011.

[54] Macey and Holdcroft, "Failure Is an Option," 1402-3.

[55] Macey and Holdcroft, "Failure Is an Option," 1338-41.

[56] Simon Johnson, "Why Won't the Federal Reserve Board Talk to Financial Reform Advocates?" *The Baseline Scenario*, February 25, 2012.

rebuttal of industry comments on the Volcker Rule.[57] Although a bright-line rule would be easier to implement and less likely to be circumvented, industry lobbyists have pushed for more exceptions and modifications on the grounds that a strict rule would undermine liquidity and raise the cost of capital—an argument that industry has successfully pushed over the efforts of consumer advocacy groups.[58]

This disparity in participatory engagement points to the second key danger of the technocratic model of regulation: it obscures the reality of the normative disputes underlying seemingly technical policy questions. This technocratic view represents an understanding of the problem of financial reform as primarily a problem of *macroeconomic management* and *market-optimization*—a conceptualization of the problem of finance that is amenable to, perhaps even demands, a policy response that privileges the role of expert oversight. In the technocratic framework, the problem of financial regulation is primarily one of market failure: financial markets are complex, and vital for economic functioning; limitations on the activities and structure of financial firms must therefore be minimalist, judicious, and most of all, devised by appeal to technical expertise. Thus, Dodd-Frank's preference for a technical approach—relying on expert regulators to manage, constrain, and respond to systemically risky firms—does not by itself solve the problem of TBTF firms,[59] where a structural bright-line rule may

[57] Rachel Signer, "Occupying the SEC for a Stronger Volcker Rule," *The Nation*, February 16, 2012; Christopher Matthews, "Occupy the SEC: Moving from the Campsite to the Weeds of Regulatory Reform," *Time Business*, February 20, 2012.

[58] Eisinger, "The Volcker Rule, Made Bloated and Weak".

[59] Macey and Holdcroft, Jr., "Failure Is an Option," 1389-90.

be more reliable in limiting firm behavior and preventing industry influence on regulators.[60]

Research, data, and expertise certainly are valuable tools for improving policymaking. But no regulatory policy can be stripped entirely of its normative commitments. By obscuring or ignoring the value considerations that implicate how raw data is interpreted and evaluated, an overly zealous recourse to expertise may have two outcomes. At worst, it risks consolidating a deeper form of "ideological capture," in which regulators share a common worldview with regulated interests but have sufficient evidence to justify decisions that are nevertheless contestable on normative grounds.[61] At best, it creates a dynamic where the real sources of legitimate disagreement are obscured. This avoidance of normative debate in turn has a chilling effect on broader political contests: the underlying sources of political debate and disagreement are obscured, leaving many affected social groups either unaware of the key implications of regulatory debates or unable to engage in the debate itself, which has retreated behind a smokescreen of technocratic discourse.

Indeed, the problem of financial reform is not merely one of technical policy design; it is also a thickly *moral* problem that involves weighty judgments about what a good economy looks like, what kinds of financial transactions are socially valuable, and about how we ought to distinguish, balance, and regulate these different kinds of activities. The degree to which an appeal to neutral expertise

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[60] Macey and Holdcroft Jr., "Failure Is an Option," 1382-3.

[61] See e.g., James Kwak, "Cultural Capture and the Financial Crisis," in Dan Carpenter and David Moss, eds., *Preventing Regulatory Capture: Special Interest Influence and How to Limit It* (New York: Cambridge University Press, 2013, forthcoming).

misconstrues morally-weighted political disagreements as merely matters of technical policy design has been noted in other areas of regulatory politics such as environmental regulation.[62] The appeal to expert judgment becomes a way to avoid rather than engage the substantive moral tensions at stake in these policy disputes. It may sound comforting to say that regulatory experts will make policy on the basis of enhancing efficiency, maximizing welfare, and mitigating risk, but these seemingly neutral, universally-acceptable goals mask very real political and moral choices that must be made in each policy issue—choices which are difficult for citizens to see let alone contest precisely because they have been construed as matters of technical policymaking, relegated to the care of financial regulatory agencies with relatively minimal roles for citizen engagement or contestation.

Financial reform as a moral and democratic challenge

The political salience and discursive limitations of risk-management and consumer protection narratives stand in stark contrast to the dynamics of the third aspiring master narrative for the financial reform debate. In place of broadly agreeable and relatively morally neutral goals such as risk mitigation and consumer protection, this third narrative cast the problem of the financial crisis not as a market failure but rather as the result of an excessive and blameworthy concentration of economic and financial *power* in the hands of the financial elite themselves. As a result, this narrative sought more structural limits on these firms as a way to ensure their accountability to the democratic public. Instead of a view

[62] See e.g., Douglas Kysar, Regulating from Nowhere: Environmental Law and the Search for Objectivity (New Haven: Yale University Press, 2010).

of regulation as a primarily expert-driven project where administrative discretion would be used to facilitate the smooth functioning of the market, these counter voices expressed a greater concern with the concentrated political and economic power of large financial firms capable of bringing down the macroeconomy—and of influencing policymakers to prevent threats to their business models. This alternative narrative thus saw the problem of finance as one of overly complex, economically concentrated financial firms like Lehman Brothers, Goldman Sachs, or Citibank, whose sheer size and interconnectedness made the survival of the entire economy contingent on these firms' success. This economic concentration in turn created the potential for these firms to abuse their place of privilege, extracting economic gains as a result of their centralized position, and in turn gaining the political influence necessary to protect their interests in Congress and regulatory bodies like the Fed. The answer to this kind of a problem of power could not be had by mere expert oversight; rather, this understanding of the problem called for more structural constraints on the organization, size, and activities of these firms.

In the early debates over regulatory reform prior to the passage of Dodd-Frank, for example, while more mainstream commentators and economists outlined proposals in line with the eventual Dodd-Frank statute—for example, calling for greater authority to the Fed as the main systemic risk regulator, promoting more coordination between regulatory agencies, or improving the expertise and professionalism of the regulators themselves[63]—this rival argument

[63] Alan Blinder, "An Early-Warning System, Run by the Fed," *New York Times*, July 25, 2009; Henry Paulson "How to Watch the Banks," *New York Times*, February 16, 2010; Scott McCleskey, "A Foreign Service for Wall Street," *New York Times*, March 20, 2010.

emerged from economists like Paul Volcker, Paul Krugman and others. Volcker famously proposed a straight ban on proprietary trading, while Krugman gradually came to call for less reliance on expert discretion, and more strict rules that would constrain the size and activities of large financial firms.[64] During her earlier work as on the Congressional Oversight Panel for the 2008-9 bank bailouts, Elizabeth Warren along with Inspector General Neil Barofsky also argued for greater structural constraints on the modern financial sector.

The most thorough articulation of this alternative narrative came from Simon Johnson, a former IMF chief economist who wrote a highly controversial and well-circulated article in *The Atlantic* in spring 2009, and continued to advocate for a more aggressive policy response to the crisis throughout the reform debate from 2009-2010. While Johnson did not view himself as a movement-builder, he explicitly framed his narrative as an heir to a populist tradition of economic and democratic reform.[65] Johnson's narrative comprised three main elements. First, instead of paying lip service to the ideal of free markets, he explicitly argued against laissez-faire economics as a self-serving ideology perpetuated by America's financial elite. According to Johnson, the financial industry "gained political power by amassing a kind of cultural capital."[66] Financial firms "benefited from the fact that Washington insiders already believed that large financial institutions and free-flowing capital markets were crucial to

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[64] See e.g. Paul Krugman, "Making Financial Reform Fool-Resistant," *New York Times*, April 5, 2010.

[65] See generally, Simon Johnson and James Kwak, *13 Bankers: The Wall Street Takeover and the Next Financial Meltdown* (New York: Vintage, 2011); Johnson and Kwak developed their ideas through a highly influential blog, The Baseline Scenario (baselinescenario.com).

[66] Simon Johnson, "The Quiet Coup," *The Atlantic*, May 2009.

America's position in the world." Far from being the default position against which reform had to justify departures, the very concept of unregulated financial markets was, for Johnson, an ideological construct favoring the interests of financial firms at the expense of the general public—a construct absorbed into the worldview of key policymakers who had spent too much time in overlapping social circles with the titans of Wall Street. Second, and relatedly, Johnson cast the problem of financial reform not as one of restoring market stability, but as a substantive and *political* clash of competing interests—in this case, a clash between Wall Street and big finance on the one hand, and the broader public on the other. Third, Johnson emphasized not only the substantive problem of how to restore equity and meaningful public oversight of the financial markets; he also cast the financial reform debate as having broader implications for the very ideal of democracy itself. The recent history of deregulation was evidence of a systemic "political balance of power that gives the financial sector a veto over public policy"—a disparity in political power that violated the ideal of democracy and had to be corrected.

Johnson's narrative provided a very different diagnosis of the financial crisis that informed a more radical solution. The policy response to the crisis, for Johnson, had to do more than simply restore financial stability; it would also have to break the political power of finance. In this account, the problem was not only one of market risk or consumer fraud. Rather, it involved the problem of concentrated economic power of financial firms, who by virtue of their economic position could exercise enormous—and ultimately unaccountable—authority over the economic fortunes of society. This threat was democratic as much as economic: the economic power of financial firms in turn came with a concentration of

political influence that posed a threat to ideals of democratic equality, while the failures of regulation leading up to the crisis highlighted further democratic concerns around the accountability and responsiveness of state officials themselves.

Thus, Johnson proposed more radical policy responses such as temporary nationalization and state-led dismantling of "too big to fail" financial firms, as well as caps on executive compensation. All these measures would be needed to "break the oligarchy" of finance. But more importantly, this alternative narrative offered greater scope for a broader shift in how citizens and policymakers alike conceive of the modern economy. By calling into question the ideology of free markets and creating a clear moral critique of the current system of high inequality, risky yet profitable financial firms, and an ailing "real" economy, the Johnson narrative opened space for a deeper debate about what a just economy ought to look like.

Just as the dominant narratives of stability and consumer protection shaped the technocratically-oriented Dodd-Frank approach, this alternative, more moralized account of the financial crisis pointed towards a more aggressive, structural type of reform. Thus, Johnson's account helped inform an array of more aggressive measures aimed at addressing the problem of TBTF through structural caps on bank size, rather than through more deferential expert oversight.

Sherrod Brown's Safe Accountable Fair and Efficient (SAFE) Banking Act proposed a strict limit to the size of big banks to $1.3 trillion in total liabilities, but had been defeated in the Senate during the Dodd-Frank negotiations.[67] Like the SAFE Act, the Kanjorski amendment to the draft Dodd-Frank statute sought to

[67] Simon Johnson, "Making Banks Small Enough and Simple Enough to Fail," The Baseline Scenario, May 20, 2012.

directly break up large financial institutions.[68] Other approaches sought to split financial firms, separating ordinary banking from securities activities, and requiring stricter oversight of potential conflicts of interest such as when Goldman Sachs could bet on the market against securities that they themselves sold to clients. These approaches, such as the Merkley-Levin amendment, were similar to the Volcker rule that made its way into Dodd-Frank, but were more aggressive in that they were statutory requirements for the breaking up of large financial firms—rather than leaving the ultimate decision to break up a firm at the discretion of the FSOC as the Volcker rule did.[69]

These proposals gained steam during the late spring of 2010, winning support among liberal Democrats[70] and earning an endorsement from the *New York Times*,[71] only to be defeated in the Congress. Ultimately, these proposals failed. The Merkley-Levin amendment did not even get to a vote in Congress, without the backing of the Democratic leadership,[72] while Brown-Kaufman was defeated in the Senate by a vote of 33-61. On the one hand, the unwillingness even on the part of the more liberal Democratic party to entertain such restrictions on banking was the product of a deep-seated faith in the technocratic expertise of regulators. The final statute did include a provision to break up systemically risky

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[68] See e.g. Simon Johnson, "A Roosevelt Moment for America's Megabanks?" Project Syndicate, July 14, 2010.

[69] "Merkley-Levin Amendment to Crack Down on High-risk Proprietary Trading," Press Release, office of Senator Jeff Merkley, May 20, 2010.

[70] David Herszenshorn, "Senate Liberals Push for Strict Financial Rules," *New York Times*, May 5, 2010.

[71] "The Hard Work on Financial Reform," Editorial, *New York Times*, May 5, 2010.

[72] *Ibid*.

financial firms—but only at the discretion of the FSOC, which itself is comprised of the leadership of the top financial regulatory agencies. Legislators thus hesitated to impose such a breakup of financial firms as a statutory rule, deferring to regulatory expertise.

Since 2010, however, these kinds of strict limits on financial firm size and activity has growing support. The Dallas Federal Reserve Bank, for example, in its 2011 annual report called TBTF financial firms a "perversion" of capitalism, increasing risks of major financial crashes without real social gains.[73] According to the Dallas Fed, by leaving TBTF institutions intact—however subject to expert regulation—Dodd-Frank was an insufficient reform effort, and needed to be supplemented by stricter limits on financial firms such that no single financial firm could be large enough to cause economy-wide repercussions were it to fail. Federal Reserve Board members Dan Tarullo and Sarah Bloom Raskin also expressed increasing support for more structural limits on TBTF firms.[74]

Financial regulation as a symptom

The financial regulation debate thus represented an attempt to respond to the excesses of market deregulation, but a problematic one that appealed primarily to a technocratic view of economic governance as expert-led risk mitigation and

[73] Federal Reserve Board of Dallas, "Choosing the Road to Prosperity: Why We Must End Too Big to Fail—Now", 2011 Annual Report, 16.

[74] Daniel Tarullo, "Financial Stability Regulation," Distinguished Jurist Lecture, University of Pennsylvania Law School, Philadelphia, PA (October 12, 2012); Sarah Bloom Raskin, "How Well Is Our Financial System Serving Us? Working Together to Find the High Road," Speech at Graduate School of Banking at Colorado, Boulder CO (July 23, 2012).

consumer protection. By contrast, the alternative democratic narrative of critics like Johnson and others had relatively little sustained political impact. Yet historically, finance and the economy more generally have been the central issues of concern for Populist and Progressive social movements, particularly during the economic upheaval of industrialization in the late nineteenth and early twentieth centuries. These movements employed narratives that were far more aggressive, substantive, and mobilizing than those of risk and consumerism. These historical narratives outlined both a causal and moral critique of private power of finance and other corporations as threats to freedom, democracy, and social welfare. They articulated a vision of an alternative political economy, one that emphasized the value of productive labor that contributed to the common good, and where the economy was structured to promote not profits but individual and collective self-realization. As such, these movements explicitly linked their narratives to deep traditions of American thought, reappropriating and redefining concepts such as freedom, democracy, and self-determination.

This disparity between the currency enjoyed by these arguments in an earlier era and their relative marginalization today is instructive. The technocratic orientation of the modern financial reform debate—its reliance on expert regulatory judgment as the preferred mode for determining socially desirable from undesirable financial activity, and its morally neutral understanding of the problem of finance in terms of risk, stability, and consumerism—actually represents the culmination of a decades-long trajectory in the discourse and conceptualization of the problem of finance. It also highlights how little our contemporary institutions work to engage and foster more mobilized democratic action beyond sporadic elections or lobbying efforts.

The following chapters trace the rise and fall of this technocratic vision, from this roots in a broader moral and democratic critique of laissez-faire during the Populist and Progressive Eras in the late nineteenth century, to its apotheosis in the New Deal, to its erosion and collapse in the face of a resurgent laissez-faire critique of the regulatory state in the late twentieth century. This trajectory underscores the appeal of technocracy as a rational and effective response to the problems of the market, its failures to overcome anxieties of its own accountability—and the degree to which this technocratic response to the market represents only one of the possible forms of economic governance oriented to overcoming the problems of laissez-faire.

3 CONTESTING THE MARKET

If the 2008 crisis undermined the claims of laissez-faire ideologues that free markets were self-correcting and socially optimal, the mainstream reform response turned to technocratic expert-led regulation to resolve market failures, mitigate risk, and protect consumers. Yet this turn to technocratic economic governance did not alleviate persisting concerns about the desirability of expert-led economic policymaking. Our modern understandings of laissez-faire and technocracy were forged through efforts to grapple with the rise of the industrial economy and the emergence of the modern regulatory state. The debate in 2008-2010 over the financial crisis took place in a conceptual terrain that itself is a product of this history. These next two chapters trace the emergence and eventual erosion of this technocratic vision as a way to better grasp its strengths and weaknesses—and to uncover the beginnings of an alternative to both markets and experts.

Specifically, this chapter examines the debates over economic governance that took place during the Progressive Era (1880-1920). Then, as now, economic upheaval prompted a rich ferment of ideas and policy innovations as thinkers and reformers struggled to respond to the rapidly changing economy. In exploring these debates, this chapter makes three points. First, the tension between laissez-faire and rival attempts at economic governance is not just about a moral disagreement over narrow understandings of freedom as the freedom to contract on the open market; it also concerns a comparative institutional claim about what kinds of decision-making systems—whether markets, or government policymakers,

or citizens—are best suited to promoting the common good, robust to the threat of corruption. Second, the motivation to develop alternative institutions for economic governance grew out of Progressive Era critiques of laissez-faire that cast the market not as a system of efficiency, but rather one of power and coercion. This critique, however, raised a further dilemma of how to respond to the problems of the market system without succumbing to the same threat of capture or corruption that laissez-faire thought highlighted. Third, in response to these concerns, Progressive Era reformers developed a variety of institutional innovations, from reforms to existing majoritarian democratic procedures to the creation of new regulatory agencies. These institutions, for reformers, were part of an attempt to make the political system itself more responsive to the general public and, in so doing, enable a more effective policy response to economic concerns. The result of these theoretical and reform debates was to generate a rich variety of institutional forms and approaches, which the later New Deal era would build on and consolidate into the modern technocratic vision of government.

Laissez-faire political thought

Advocates of laissez-faire thought in the late nineteenth century articulated a vision of economic governance comprised of three central elements. First, state regulation of the economy was acceptable through the development of judge-made common law doctrines and the use of state police power, which were regularly employed to promote economic development and public welfare. Second, the limitations on state action arose not from a rejection of state action *per se*, but from a concern with political corruption: where the state seemed to promote the

partial interests of a particular social group or class, such state actions would be illegitimate. The preference for market-based social order thus emerged in part out of a search for an institutional form of social order that was robust against the self-interest of competing social groups. Third, this framework of laissez-faire thought rested on—and helped consolidate—an underlying understanding of freedom as individual liberty from constraint, in particular the liberty to engage in market transactions as an autonomous agent. Although these thinkers held to a view of freedom as freedom from state interference, they did not entirely reject the idea of the state in economic regulation. The laissez-faire vision, then, was not a naked appeal to libertarianism or unrestrained markets, but rather a fundamentally moral, institutionally sophisticated, and even reformist effort to secure liberty and public welfare against corruption. This more nuanced tradition of laissez-faire persisted into the current era as a recurring critique of efforts to expand the scope of economic regulation, and formed the primary villain against which Progressive reformers had to mobilize.

Laissez-faire, regulation, and the fear of capture

Private common law during the early nineteenth century developed through explicit debates over what kinds of legal doctrines would best promote economic development and a good economy. State judges reworked standards of legal injury and damages to better promote economic development. For example, judges defined tort doctrines to allow for some interference with landed property rights if it resulted in improved economic production, such as through the construction of a

new mill or dam.[1] Judges made explicit comparisons of the relative social value of different property uses to determine legal injuries.[2] Nuisance doctrine also shifted to more flexible negligence standards, enabling courts to limit the scope of legal damages faced by emerging industries and their impact on the environment and nearby citizens.[3] At the same time, judges during this period increased legal protections for corporations, through the development of classical corporate personhood doctrines that recognized corporations' rights against the state and other persons. These legal developments were explicitly geared towards protecting the corporate form of association as a more efficient method of channeling business capital, encouraging investor confidence, and promoting development.[4]

These trends in private common law took place alongside a robust tradition of "police power"—the sovereign authority of states to provide for health, welfare, and other socioeconomic regulation. As William Novak argues, state governments engaged in a variety of social and economic regulations aimed at promoting substantive visions of the good life:

> The nineteenth century was not an era of laissez-faire or statelessness where public inertia and political naiveté just happened to provide the perfect conditions for a burgeoning private market economy and a self-generating civil democracy. On the contrary, the fundamental social and economic relations of the nineteenth century—the market, the city and the countryside, the family, the laborer, the proprietor, the good neighbor, the

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[1] See e.g., *Palmer v. Mulligan*, 3 Cai. R. 307 (1805); *Platt v. Johnson*, 15 Johns. 212 (NY 1815).

[2] Morton Horwitz, *The Transformation of American Law, 1780-1860* (Cambridge: Harvard University Press, 1977), 32-8.

[3] See e.g., *Callender v. Marsh*, 1 Pick. 418 (Mass. 1823); Horwitz, *Transformations 1780-1860*, 67-71, 85-99.

[4] Herbert Hovenkamp, *Enterprise and American Law, 1836-1937* (Cambridge: Harvard University Press, 1991), 11-64; Howard Gillman, *The Constitution Besieged: The Rise and Demise of Lochner Era Police Powers Jurisprudence* (Durham: Duke University Press, 1993), 47-8.

> good citizen—were formed and transformed in this period as the constant objects of governance and regulation.[5]

This practice of police power governance looks very different from the myth of a rigid emphasis on individual liberty, free markets, and limited government. Instead, police powers jurisprudence saw individuals as socially-embedded, with rights that were ultimately relational rather than absolute. In this setting, the common law was a dynamic, man-made policy tool essential to realizing—rather than merely constraining—the common good and public welfare.[6] Judges, lawyers, and commentators alike during this period "envisioned not a defensive society and government, summoned to action sporadically when individual rights were endangered, but a public society in motion, ever reaching to secure the general welfare, public happiness."[7] State courts routinely supported social and economic regulations arising from the exercises of the state legislature's police power, upholding the construction of public spaces, waterways, and roads; the imposition of fire regulations trumping claims to absolute property rights by landowners; public health and safety regulations for cleanliness; and economic regulations over trade, occupational licensing, and product safety.[8]

The economy was thus seen as "fundamentally public in nature, created, shaped, and regulated by the polity via public law."[9] Nineteenth century thinkers and judges accepted some regulation of businesses that were uniquely "affected

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[5] William Novak, *The People's Welfare: Law and Regulation in Nineteenth Century America* (Chapel Hill: University of North Carolina Press, 1996), 236.

[6] Novak, *The People's Welfare*, 26-45.

[7] Novak, *People's Welfare*, 45.

[8] Novak, *People's Welfare*, 51-87.

[9] Novak, *People's Welfare*, 84.

with the public interest" as legitimate, alongside other protections for morals, health, and safety.[10] Even later where laissez-faire thinkers advocated for individualism in the economic realm, they proved broadly accepting of government regulations to facilitate growth, curtail alcohol consumption, and restrict individual liberties in the name of morality, such as through blasphemy laws.[11] Even grants of private corporate charters were often narrowly construed by courts to ensure that corporate authority remained consistent with what the courts understood to be the public interest.[12] Of course, this still left a wide degree of latitude for courts to construe their understanding of the common good and public welfare in particular ways, including granting greater leeway for emerging industries against the claims of other citizens. Nevertheless, this discourse accepted a major economic role for the state and for regulation. The debate was not over whether or not law *could* regulate aspects of social and economic activity, but how law *should* do so. Much of this framework was conducive to economic reform politics, and indeed later reformers like Louis Brandeis explicitly positioned themselves in the police powers tradition.

Given the scope of acceptable regulation, the limitations on the state in laissez-faire thought emerged not from an outright rejection of state regulation, but rather from a more nuanced understanding of nineteenth century political economy that sought to immunize public politics from the danger of partial

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[10] Michael Les Benedict, "Laissez-Faire and Liberty: A Re-Evaluation of the Meanings and Origins of Laissez-Faire Constitutionalism," *Law and History Review* 3:2 (1985), 293-331, at 304.

[11] See Herbert Hovenkamp, "The Classical American State and the Regulation of Morals," Draft, April 2012, on file with author.

[12] Novak, *People's Welfare*, 105-9.

legislation favoring particular private interests over the common good. The nineteenth century preference for the market as the mode for organizing social behavior thus emerged as a result of a *comparative institutional assessment*: the market, in this view, was robust against the partial preferences of self-interested groups, generating socially-optimal results through autonomous bargaining and fair transactions. By contrast, state action risked promoting the interests of some segments of society over others, through the likelihood of political corruption and legislative capture. Where the state could be shown to regulate in the general interest through police power or common law, these exercises of political authority were acceptable, but otherwise the market seemed a more optimal and corruption-free mechanism for social progress.

Thus, in the early 1800s, regulation was viewed skeptically insofar as it was seen to benefit particular classes and their property or investments. The Jacksonian hostility towards regulation and the development of the classical view of laissez-faire—that emphasized limited governmental powers especially in economic regulation, along with the principle of equal access to economic opportunities—grew out of this core skepticism of favoritism.[13] The greatest threat to liberty came from the "temptation to misuse the powers of government for the benefit of those who controlled it."[14] Because of the influence of the rich or powerful, special privileges were seen as presumptively inequitable.[15] As the scope of economic regulation increased over the mid-nineteenth century, there were more

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[13] Hovenkamp, "The Classical American State," 3-4.

[14] Les Benedict, "Laissez-Faire and Liberty," 306.

[15] Les Benedict, "Laissez-Faire and Liberty," 319-20 (citing the example of legal scholar Thomas Cooley's writings).

legal attacks on state and then federal economic regulations as exceeding legislative powers. The judicial response to these challenges revolved around a back-and-forth debate over whether the regulation in question favored one particular interest over the common good.[16]

As Howard Gillman argues, "nineteenth-century courts were on guard against not all regulations of the economy but only a particular kind of government interference in market relations—what the justices considered 'class' or 'partial' legislation; that is, laws that (from their point of view) promoted only the narrow interests of particular groups or classes rather than the general welfare."[17] When judges struck down legislation and regulation, it was not out of a rote adherence to free market ideology, but rather out of a particular—and often nuanced—understanding of political economy and political legitimacy, upholding legislation that seemed to them as general and pursuant to the public good, and striking down legislation which seemed to advance the particular interests of certain groups unfairly.[18] This ideal of 'faction-less politics' as the standard characterizing legitimate exercise of the police power yielded a judicial preference for generally-applicable legislation treating all citizens equally. The constraints on state action in this framework, then, were not simply the result of an outright rejection of the idea of regulation or economic intervention. Rather, the limitations on state action came out of a fundamentally *political* concern about accountability and the public good.

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[16] See e.g., *Slaughterhouse Cases*, 83 U.S. 36 (1872); *Munn v. Illinois*, 94 U.S. 113 (1876); *Yick Wo v. Hopkins*, 118 U.S. 356 (1886); *Powell v. Pennsylvania*, 127 U.S. 678 (1888).

[17] Gillman, *The Constitution Besieged*, 7.

[18] Gillman, *The Constitution Besieged*, 10.

Indeed, late nineteenth century advocates of laissez-faire—including academics like William Graham Sumner, Lyman Atwater and Arthur Perry, businessmen like Edward Atkinson, and journalists like E. L. Godkin—often did not see themselves as mainstream, but rather as reformers pushing against the tide of corruption and special legislation through steady advocacy, argumentation, and persuasion.[19] Herbert Spencer, who became one of the most influential advocates of laissez-faire, combined these elements of negative liberty and distrust of legislators to argue for limited government and freedom of exchange through treatises and pamphlets popularized by organizations like the American Free Trade League.[20] These arguments were eagerly absorbed and further advocated by businesses, especially in their efforts to prevent the growing movement towards labor legislation.[21]

Consolidating laissez-faire: legal formalism and market freedom

The result of all this ferment was the development of an entrenched legal theory of limited legislative and economic regulatory authority on the part of the state, which gained traction not on ground of outright rejection of the state, but because of the fear of "class" legislation favoring particular special interests.[22] Laissez-faire thought thus combined an acceptance of some forms of state

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[19] Les Benedict, "Laissez-Faire and Liberty," 306.

[20] See Sidney Fine, *Laissez-Faire and the General Welfare State: A Study of Conflict in American Thought*, 1865-1901 (Ann Arbor: University of Michigan Press, 1956), 33-39, 47-51.

[21] Fine, *Laissez-Faire and the General Welfare State*, 115-7.

[22] Les Benedict, "Laissez-Faire and Liberty," 327-31 (citing especially Thomas Cooley and John Dillon as examples).

regulation, with a distrust of special interests and corruption. It was only later that these ideals were absorbed by and came to be affiliated with the interests of big business and the wealthy.[23] But as these understandings of economic governance were being increasingly formalized in law and late nineteenth century thought, structural changes in the economy and society were increasingly voiding these very assumptions of freely competitive markets. These conceptual elements congealed into an increasingly rigid legal and conceptual framework of laissez-faire political economy, which served as the chief constraint against which later Populist and Progressive reformers would clash.

Over time these political concerns about capture and effectiveness helped drive the consolidation of laissez-faire political economy into more rigid doctrines of law and negative understandings of freedom. While the police powers jurisprudence emerged more out of the day-to-day practice of governing rather than high theorizing, eventually deep disagreements over competing visions of the good society led to a rejection of this tradition of regulation.[24] By the 1850s, judicial dissents against the exercise of police power appeared with greater frequency, driven by newfound cynicism over the public spiritedness of local officials and their propensity to captured by powerful, and partial interest groups.[25] Meanwhile, business interests, having secured effective legal subsidies through shifts in common law doctrines, increasingly attempted to "lock in" these gains, recasting the more functional and policy oriented doctrines of the early nineteenth

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[23] Les Benedict, "Laissez-Faire and Liberty", 311-13.

[24] Novak, *People's Welfare*, 8-17.

[25] Novak, *People's Welfare*, 102.

century in terms of legal formalism. The doctrines that had initially emerged as conscious policy decisions to promote economic development were increasingly recast as the results of neutral legal principles, discerned and implemented by an increasingly autonomous, professionalized legal system.[26]

This framework of classical legal thought thus came to operate as a handmaiden to laissez-faire conceptions of market and state. The goal was to "create a sharp distinction between what was thought to be coercive public law—mainly criminal and regulatory law—and non-coercive private law of tort, contract, property, and commercial law, designed to be resistant to the dangers of political interference."[27] This distinction between public and private law "sought to establish a separate 'natural' realm of non-coercive and non-political transactions free from the dangers of state interference and redistribution."[28] This distinction between a natural, self-organizing domain of private law and free market transaction on the one hand, and coercive state power in criminal and regulatory law on the other, operated to provide a check on state authority. In effect, classical legal thought depoliticized and formalized what had been a more permissive and instrumental understanding of law and state regulation of the economy.

As it congealed and became more formalized, the laissez-faire paradigm of economic governance bundled the emphasis on promoting the public good by promoting economic development, with a suspicion of state action particularly

[26] Horwitz, *Transformation 1780-1860*, 254-9.

[27] Morton Horwitz, *The Transformation of American Law, 1870-1960* (New York: Oxford University Press, 1992), 10-11.

[28] Horwitz, *Transformations 1870-1960*, 11.

with respect to the risk of private interests and institutional capture. The resultant view of the market as "an arena of self-equilibriating, moral freedom" emerged in large part out of a reaction against the threat of political corruption.[29] The aversion to factional politics itself rested on the background assumption that no segment of society—not even increasingly marginalized groups such as workers in the mid- to late-nineteenth century—needed special protections. In this setting of autonomous individuals, liberty was best promoted by the free market; state regulation was acceptable, but only for the general welfare. Specific protections for particular segments of society were transgressions against this narrower market-based conception of freedom and its commitment to class neutral general legislation. As Gillman notes,

> So long as people continued to believe that their well-being could be ensured by a harmonious market uncorrupted by the imposition of artificial government burdens or benefits, there was little reason to question the legitimacy of the ethos of the neutral policy.[30]

The key actors in maintaining and implementing this vision of laissez-faire economic governance were the judiciary and the bar. As Stephen Skowronek notes, courts, alongside political parties, were one of the primary central nationally-integrated policymaking systems in American society. They defined state-society relations, especially in the domain of economic policy through the regulation of corporate charters, state action, and doctrines of substantive due process.[31] Lawyers and judges themselves emerged as an expert class of self-

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[29] Daniel Rodgers, *Atlantic Crossings: Social Politics in a Progressive Age* (Cambridge: Harvard University Press, 1998).

[30] Gillman, *The Constitution Besieged*, 39.

[31] Stephen Skowronek, *Building a New American State: The Expansion of National Administrative Capacities, 1877-1920* (New York: Cambridge University Press, 1982), 24-7

conscious policymakers working through the domain of law to police the boundaries of legitimate state action.[32] Law was thus one of the key terrains in which these ideas of political economy battled. Laissez-faire became embedded in legal doctrine through the debates of the mid- to late-nineteenth century, captured in the treatises of influential legal scholars like Thomas Cooley and John Dillon, who argued for implied legal limits to the police powers of states when it came to economic regulations.[33]

Meanwhile, the landmark Supreme Court case of *Lochner v. New York* (1905)[34] exemplified the judiciary's hostility to Progressive reform, as the court narrowly struck down a New York state law imposing standards for the length of the workday in bakeries. The Court reasoned that the regulation was the result of worker interests capturing the state legislature, rather than expressing a general public interest. Yet, the Court also upheld various state efforts to regulate railroad rates through the Granger laws. The *Lochner* court was motivated by this laissez-faire view of economic governance, which accepted some role for state-fostered economic development, but was highly averse to the appearance of class politics. As legal histories of the period suggest, the Court in general attempted to distinguish between special burdens imposed on segments of society that were necessary for the general welfare, and class legislation that unfairly and illegitimately discriminated against some in favor of others.[35] If individual citizens

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[32] Skowronek, *Building a New American State*, 31-4, 43-4.

[33] See Les Benedict, "Laissez-Faire and Liberty"; Fine, *Laissez-Faire and the General Welfare State*, 128-35.

[34] *Lochner v. New York*, 198 U.S. 45 (1905).

[35] Gillman, *The Constitution Besieged*, 72.

were seen as independent, in general not posing a threat to one another, then the market could be seen as a system of free and equal exchange, and an equitable institutional system for adjudicating the rival interests.[36] Under such background conditions, any legislation that seemed to focus on a particular segment of society was presumptively illegitimate. *Lochner* thus represented neither judicial corruption nor libertarian ideology, but rather a clash between the laissez-faire economic governance and the changed socioeconomic reality that provoked new legislative efforts to protect special groups seen as vulnerable.[37] The *Lochner* court saw itself as protecting against legislative corruption by partial interests of workers, while reformers saw themselves as protecting the public in the face of a new industrial economic order.

The challenge for reformers

Yet precisely at the moment that *Lochner* expressed this laissez-faire view of the economy, it was becoming increasingly clear that various segments of society would need state intervention to help counter the pressures of rising corporations and market instability.[38] *Lochner* was just one of the most famous flashpoints between defenders of laissez-faire and growing efforts to remake the economic order in the face of the rise of large corporations and the dislocations of industrialization.

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[36] See Gillman, *The Constitution Besieged*, 61-4.

[37] Gillman, *The Constitution Besieged*, 11.

[38] Gillman, *The Constitution Besieged*, 63-4.

Social movements such as the trade union movement, the Knights of Labor, the Grangers, and the Populists, emerged to defend the freedom of workers, farmers, and other segments of society, but these collective responses to industrialism were largely viewed by the judiciary as illegitimate class politics, any form of legislative capture privileging the interests of the few over the many.[39] Furthermore, legislation favoring these groups seemed to offer no general benefit to broader society. Thus, courts often applied tougher standards against labor than against business, for collective action by labor was seen as a source of instability, efficiency, and undue political power with no offsetting gains from economies of scale, whereas some combinations of business could be defended as contributing to the overall economic welfare of society.[40] Indeed, most legal treatises of that era actually saw existing public policy as overly solicitous of worker and labor interests.[41]

These elements—a fear of corruption, a narrow view of negative liberty, sustained by legal doctrine—combined into a coherent worldview that suffused mid-nineteenth century understandings of politics and markets, given further force and effect through their codification in legal jurisprudence. As such, this laissez-faire paradigm of political economy constrained reformists' efforts at both a conceptual and legal level. Progressive Era thinkers thus had to overcome a dual challenge. First, they had to reveal the notion of free markets as an illusion, highlighting the realities of coercion, power, and social harm that took place under

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[39] Gillman, *The Constitution Besieged*, 86-93.

[40] Hovenkamp, *Enterprise and American Law*, 208-222.

[41] Hovenkamp, *Enterprise and American Law*, 211-3.

the guise of 'free markets'. Second, they had to develop alternative institutions that could govern the modern economy in a way that better promoted the common good—but did so while also avoiding the kinds of special interest influence and corruption that laissez-faire thought warned would be endemic in the turn to state economic regulation.

The Progressive critique of laissez-faire

The dramatic changes to the American economy in the late nineteenth century provided a catalyst for reform movements and new intellectual thought. Ordinary citizens increasingly found themselves at the mercy of the modern economy, subordinate to and dependent upon powerful private entities such as railroad monopolies, financial firms like J.P. Morgan, and trusts like Standard Oil. At the same time, the vast impersonal forces of the market itself created widespread anxiety and hardship through social dislocation, fluctuating wages, and volatile commodity prices. Industrialization, urbanization logical change threatened not only the stability of professions but also basic health and safety in and outside of the workplace. These anxieties were experienced by large swaths of Americans society, from farmers to industrial workers to the urban middle-class. Old ideals of individual liberty and independence secured through free contract suddenly seemed irrelevant. But to address these concerns, reformers had to first overcome the intellectual edifice of laissez-faire thought. Progressive Era thinkers thus focused their arguments on deconstructing this vision of markets as smooth, corruption-free systems.

Progressive Era reformers approached their critique of laissez-faire in three ways. First, a group of Progressive thinkers and legal scholars loosely known as the 'legal realist' movement challenged conventional understandings of laissez-faire by highlighting the ways in which the seemingly natural dynamics of market society were in fact the product of coercion between private actors. As such, the supposedly free market generated moral and social harms that had to be remedied—particularly harms from the concentrated power of private actors like firms, and the harms from the diffuse aggregate dynamics of market forces. Second, these thinkers also argued that the market economy was a fundamentally political institution, suffused with background regulation by the state through laws of property, contract, and tort—and thus was already subject to social control. Third, if the market was in fact the product of such coercion and endemic state action, as these thinkers argued, then, rather than shying away from the power of the state as something to be eliminated, this power should instead be harnessed to promote a more frank and openly discussed public good.[42] The response to both of these threats of private and market power was through revived and reformed political institutions that could alter the dynamics of the market itself to better promote social welfare.

The first threat posed by market society was the problem of private power. This problem was most glaringly posed by the rise of large corporations and trusts during the late nineteenth century, comprising the chief villain for antitrust reformers. As one of the intellectual leaders of the Progressive movement, Louis Brandeis best articulated this concern with private power as a threat to individual

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[42] See generally, Joseph Singer, "Legal Realism Now," *California Law Review* 76:2 (1988), 465-544; Horwitz, *Transformations, 1870-1960*.

freedom and social welfare. Large corporations, to Brandeis, enjoyed profits while paying less than subsistence wages, creating a disparity in political power that was akin to slavery where workers were "absolutely subject" to the will of the corporation.[43] The contrast of enormous profits for corporate entities such as the Steel Trust with the lack of subsistence wages for workers was for Brandeis symptomatic of a vast disparity of power that amounted to a form of industrial slavery.[44] These large corporations effectively enjoyed a power bordering on "industrial absolutism," which Brandeis argued was irreconcilable with American traditions of political liberty.[45] Even if corporations acted benevolently towards their workers and towards consumers, the unaccountable power possessed by these corporations was such that they constituted a coercive state-like entity "so powerful that the ordinary social and industrial forces existing are insufficient to cope with it."[46] Although these private firms had acquired power to rival the state, they lacked the political checks on the exercise of such power that come with state authority. Because of this risk of unaccountable arbitrary power, these private firms were dangerous, even if their power was used benevolently.[47] Such concentrated private power, for Brandeis, comprised the "greatest problem" facing

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[43] Louis Brandeis, "Big Business and Industrial Liberty," in Osmond Fraenkel, ed., *The Curse of Bigness: Miscellaneous Papers of Louis Brandeis* (New York: Viking Press, 1935), 38-39, at 39.

[44] Brandeis, "Big Business and Industrial Liberty," 38-9.

[45] Brandeis, "On Industrial Relations," testimony to Congress, January 23, 1915; in Fraenkel, ed., *Curse of Bigness*, 70-95, at 72.

[46] Brandeis, "On Industrial Relations," 73.

[47] Louis Brandeis, *Other People's Money, And How the Bankers Use It* (New York: Frederick Stokes, 1914), 80.

American citizens: "the problem of reconciling our industrial system with … political democracy."[48]

Investment bankers like JP Morgan were the particular villains of Brandeis' account, for they controlled not only their own vast wealth, but also the wealth of everyone else.[49] This "money trust" of "banker-barons" created evils for society such as higher tolls and prices for services, weakening of competition and innovation, and the "suppression of industrial liberty."[50] The concentrated economic power of these financial interests meant that they could affect anyone dependent on them for credit or for sustaining a market for the self-produced goods of farmers and entrepreneurs. All of modern society thus lay under the domination and arbitrary will of financial giants.

Similarly, Louis Jaffe argued that private trade groups and corporations effectively created *law* by generating standard practices and customs though these were nominally 'private' entities. In effect, "the state has relinquished to the individual the 'sovereign' function of laying down the rules which govern society."[51] For Jaffe, associations and corporations could legitimately make their own rules, but when they reached a certain size, they acquired coercive authority over others—for example, unions that could bar trade with certain parties, or corporations who could set the terms of wage and labor practices:

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[48] Brandeis, "Industrial Cooperation," address before the Filene Cooperative Association, Boston, May 1905, in Fraenkel ed., *Curse of Bigness*, 35-37, at 35.

[49] Brandeis, *Other People's Money*, 12-13.

[50] Brandeis, *Other People's Money*, 34.

[51] Louis Jaffe, "Law Making by Private Groups," (1937), in William W. Fisher III, Morton Horwitz, Thomas Reed, eds., *American Legal Realism* (New York: Oxford University Press, 1993), 115-120, at 116.

> Great complexes of property and contract which constitute our modern industrial machine, the monopolistic associations of capital, labor, and the professions which operate it, exert under the forms and sanctions of law enormous powers of determining the substance of economic and social arrangements, in large part irrespective of the will of particular individuals.[52]

Such private power posed a major problem in democratic society, for its nominally "private" nature insulates it from the kinds of political checks that constrain and direct equally coercive state power:

> Tolerated, covert monopolies—power exercised indirectly—may be much more difficult to attack or to ameliorate than the edicts of majorities arrived at openly and according to the forms of law.[53]

These threats to individual freedom and wellbeing were not limited to large corporations and monopolies. Indeed, Progressive Era thinkers saw a spectrum of private power running from the highly visible monopolies and trusts, to more diffuse forms of private power exercised throughout the market economy. Thus, by the 1920s, it became clear to many Progressive thinkers that the seemingly free domain of private market transactions was actually riven by power imbalances between private market actors such as firms and workers. The aggregation of such exercises of power created the seemingly impersonal forces of "the market."

This critique of market power was advanced particularly powerfully by the legal realist school of thought that emerged during this period. For the legal realists, market outcomes were not merely efficient results of fair transactions. Rather, they were outcomes in large part determined by the prior distribution of bargaining power in society–distribution which was fundamentally created and thus alterable by the state through enforcement of background legal doctrines of

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[52] Jaffe, "Law Making by Private Groups,"119.

[53] Jaffe, "Law Making by Private Groups," 120.

contract, property, and tort. The free market itself was thus effectively a regulatory system created by the state through law. Therefore, it could be reshaped through state control to realize more explicit policy goals and normative aspirations.[54]

Robert Hale, for example, argued that because coercion was omnipresent even in free market society, state power was already in some sense present in the private domain of market transactions. "The distribution of income," argued Hale, "depends on the relative power of coercion which the different members of the community can exert against one another."[55] But the coercive powers of private individuals themselves derived from state-sanctioned structures of property and contract rights. Thus, rather than accepting existing distributions of income or private power as "natural," reformers could change these distributions, provided they had a coherent theory to guide and structure this already-present role of the state in the economy. This blurring of the distinction between state power and private power was vital to enabling more open policy interventions aimed at economic ills such as income inequality or low wages. Morris Cohen similarly argued that property was itself a form of sovereign power, compelling obedience in the commercial economy just as state power compelled obedience in politics.[56] As a result, "it is necessary to apply to the law of property all those considerations of social ethics and enlightened public policy which ought to be

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[54] See generally, Horwitz, *Transformations 1870-1960*, 193-4, 206-8; Singer, "Legal Realism Now," 495.

[55] Robert Hale, "Coercion and Distribution in a Supposedly Non-Coercive State" (1923), in Fisher et. al., eds., *American Legal Realism*, 101-8, at 108.

[56] Morris Cohen, "Property as Sovereignty" (1927), in Fisher et al, eds., *American Legal Realism*, 109-114.

brought to the discussion of any just form of government."[57] The legal realists' "attack on the public/private distinction was the result of a widespread perception that so-called private institutions were acquiring coercive power that had formerly been reserved to governments."[58]

Beyond particular coercive transactions and unfair bargaining positions in, for example, wage levels, the aggregate dynamics of the market itself posed a broader, systematic threat to individual liberty and social welfare. Thus, while John Dewey shared the legal realist critique of 'free markets' as structured by the coercive operation of property and contract rights, for Dewey the market posed an even bigger threat. According to Dewey, in the modern economy, the central constraint on individual flourishing was not the state, but rather "material insecurity" and "the coercions and repressions that prevent multitudes from participation in the past cultural resources that are at hand."[59] The market, for Dewey, created broader instabilities, externalities, and risks that affected those far beyond the binary transactional relationships of private exchange. What was most pernicious about this market system was that the *cumulative* effect of individual market transactions had repercussions affecting a wider range of citizens, for example through aggregated fluctuations in wages and prices, or through the imposition of what today we would think of as externalities—risks to health, safety, and the like. These risks were especially dangerous because they defied the ability of any one individual to contest them. A worker facing low wages as a

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[57] Cohen, "Property as Sovereignty," 114.

[58] Morton Horwitz, "The History of The Public/Private Distinction," *University of Pennsylvania Law Review* 130 (1982), 1423-1428, at 1425.

[59] John Dewey, *Liberalism and Social Action* (New York: Prometheus, 2000), 54.

result of market competition could not, as an individual, seek redress from any one other actor, as the condition of wage risk was a product of thousands of aggregated transactions far beyond the knowledge and reach of the worker.

Nor was this critique of the market generated solely by philosophers and lawyers. Much of the intellectual energy of the growing social science and economics community was directed towards this Progressive challenge of overcoming laissez-faire thought through what these thinkers saw as a more accurate and realistic understanding of modern society. Economists like E. R. A. Seligman drew on newly emerging theories of marginal utility and diminishing returns to argue for a graduated income tax on the grounds that the wealthy simply derived fewer welfare gains from each marginal dollar of income than the poor—thus challenging Supreme Court rulings that had cut down reforms aimed at increasing taxes on the wealthy.[60] Other economists like John Commons argued in defense of labor unions as a way to maximize workers' ability to be paid a fair wage, which Commons defined by appeal to economic science as equivalent to the workers' marginal contribution—plus some additional element to achieve social welfare-enhancing redistribution. Here too, Commons clashed with prevailing Supreme Court precedents that struck down reformist efforts at achieving a minimum wage.[61] Finally other economists like Richard Ely and Thornstein Veblen lent additional weight to the legal realist critiques of market contracting and bargaining as fundamentally unequal.[62] These economists all shared a view of

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[60] See Herbert Hovenkamp, "The First Great Law and Economics Movement," *Stanford Law Review*, 42:4 (1990), 993-1058, at 1000-9.

[61] Hovenkamp, "The First Great Law and Economics Movement," 1010.

[62] Hovenkamp, "The First Great Law and Economics Movement," 1022-23.

the market not as a naturally occurring state, but rather as a social institution, that could and should be modified to promote social welfare.[63] Where later economics would serve as a launching pad for the laissez-faire revival and a modern critique of the regulatory state in the late twentieth century, during the Progressive Era economists provided one of the key intellectual bulwarks for the critique of laissez-faire.

This critique implied the need to develop equivalent checks and norms to limit and shape the actions of these private and market actors. In such a setting of private and markets based coercion, the neutral state could no longer justifiably sit apart from the task of economic regulation. Rather, state policy would be needed to help balance disparities in power and opportunity. By the 1920s, this argument gained traction as "more and more judges and lawyers were trying on the progressive notion that the general welfare in the age of industry require the government to expertly adjust and manage tumultuous market relations"—thus undercutting the "linchpin" of traditional laissez-faire jurisprudence which sought to distinguish between valid legislation for the general welfare and invalid legislation promoting the interests of particular groups such as workers.[64]

Building a new democracy

This broad socioeconomic crisis mobilized an entire generation of reformers and thinkers during the Progressive Era. Concerned with the rise of concentrated private power, monopoly, and the dislocations and uncertainties of the market,

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[63] Hovenkamp, "The First Great Law and Economics Movement," 1023-29.

[64] Gillman, *The Constitution Besieged*, 149-150.

these reformers sought to create an alternative economic order. From rural farmers and factory workers to a growing class of intellectuals and social scientific reformers, the period represented one of the richest moments of debate over the nature and structure of American political economy. While impossibly diverse in demographics, proposals, and organizational forms, at its heart all of this mobilization focused around the core question of how to govern the new industrial economy. Activists, reformers, and thinkers grappled with competing visions of politics, state-society relations, and economic order.

But the task of reform faced another barrier in the limitations of existing political institutions. Many reform proposals were out of sync with limited federal and state governmental capacity to regulate the dynamics of industrial capitalism. Courts constrained the very political terrain in which reformers could mobilize, act, and innovate.[65] Legislatures and political parties seemed increasingly corrupt, and beholden to the very private interests that reformers sought to constrain. The multiplication of social interests arising from the newly industrializing economy seemed to threaten the ideal of a coherent public good to be realized by state action.[66] The problem of capitalism, for Progressives, was thus fundamentally a problem of politics. To better control, redirect, and respond to the challenges of industrial capitalism, these reformers had to overcome these political blockages in an attempt to unleash their own capacities as self-governing citizens.

The Populist movement of rural reformers, for example, sought to challenge growing corporate power, inequality, and the vagaries of the modern market

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[65] See Skowronek, *Building a New American State*, 122-139.

[66] Richard McCormick, "The Discovery that Business Corrupts Politics: A Reappraisal of the Origins of Progressivism," *The American Historical Review*, 86:2 (1981), 247-74, at 251-57.

system both by demanding more responsive government institutions and expanding the capacity of farmers themselves to engage in self governance and political action. Reformist farmers saw themselves as pitted against key villains of their contemporary political economy: middlemen whose markups raised costs and lowered profits for farmers, and railroads and financial firms whose monopolistic control enabled them to charge unfair rates for transport and credit.[67] The central concern for the Populist movement was the threat that private power posed to individual liberty, a deep anxiety that such private dominion would displace democracy and leave individuals powerless and enslaved: "populists feared that sovereignty would reside in the private realm and that this would lead to a class-state under the dominance of business."[68] In response, the Populists engaged in a broad effort to educate and mobilize rural farmers, building a network of decentralized protest. The electoral aspirations of these movement were secondary—and therefore ultimately limited.[69] Populists sought to restore some form of citizen control over the forces of the modern market system, through a combination of political advocacy, institution building, and mobilization of farmers themselves. Through organizations such as the Farmers Alliance, farmers advocated for government regulation and public ownership of railroads and credit, while engaging in massive civic education campaigns aimed at improving the livelihood and political skills of ordinary rural citizens.[70] As Charles Postel argues,

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[67] Charles Postel, *The Populist Vision* (New York: Oxford University Press, 2007), 116-7.

[68] Norman Pollack, *The Just Polity: Populism, Law, and Human Welfare* (Urbana: University of Illinois Press, 1987), 5.

[69] See Pollack, *The Just Polity*, 17-25.

[70] Postel, *The Populist Vision*, 10-20.

"participants in this movement believed that they could collectively wield new technological and organizational methods … [and] efforts of common citizens to shape the national economy and governance."[71]

Though a largely urban, middle-class movement, Progressive reformers similarly sought to respond to the problems of concentrated corporate power in the form of trusts, decentralized market power that gave rise to problems such as poverty, and the ongoing political challenge of corruption within state legislatures, the main political parties, and the seemingly business friendly judiciary.[72] Progressives have often been derided as racially-exclusive; a movement of middle-class elites espousing socially conservative Victorian sensibilities;[73] prone to favor corporate capitalism[74] and bureaucratic, organizational mastery. Many of these criticisms are deserved. But the Progressive movement was also highly diverse, and built a rich reform discourse around a shared core focus on the threat of unregulated power in the marketplace.[75]

The breadth and diversity of reform politics in this era necessarily meant that there were conflicting currents amongst reformers. Although these reformers

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[71] Postel, *The Populist Vision*, 4.

[72] See e.g. Sidney Milkis, "Progressivism, Then and Now," in Sidney Milkis and Jerome Mileur, eds., *Progressivism and the New Democracy* (Amherst: University of Massachusetts Press, 1999), 1-39; Don Kirschner, "The Ambiguous Legacy: Social Justice and Social Control in the Progressive Era," *Historical Reflections* 2:1 (1975), 69-88.

[73] See e.g. Michael McGerr, *A Fierce Discontent: The Rise and Fall of the Progressive Movement in America, 1870-1920* (New York: Free Press, 2003).

[74] Martin Sklar, *The Corporate Reconstruction of American Capitalism: 1890-1916: The Market, the Law, and Politics* (New York: Cambridge University Press, 1988), James Livingston, *Origins of the Federal Reserve System: Money, Class, and Corporate Capitalism, 1890-1913* (Ithaca: Cornell University Press, 1986).

[75] Daniel Rodgers, "In Search of Progressivism," *Reviews in American History*, 10:4 (1982), 112-132, at 117-27; Morton Keller, *Regulating a New Society: Public Policy and Social Change in America, 1900-1933* (Cambridge: Harvard University Press, 1994), 1-6, 180-214.

did not ultimately agree on what kind of politics would be ideal, they collectively experimented with a range of new political institutions. The result was a rich innovation in a variety of new political institutions, from direct democratic referenda to the creation of new regulatory agencies. What linked these innovations together was that they all sought to enable policies that could better respond to economic upheaval, but specifically sought to do so through processes that would be more immune to the threat of corruption and capture. Thus, Progressives during this time saw in the idea of empowering "the people" through direct democracy and pursuing the common good through expertise and regulation as ways to solve this dual problem of economic change and special interest or elite political influence.

Majoritarian democracy and mobilization

The first major front for institutional innovation during this period was the attempts to rescue majoritarian electoral democracy from cooptation by economic and political elites.

From 1890 to 1912, Progressive reformers succeeded in institutionalizing the first ballot, recall, initiative, and referenda procedures in state constitutions. This turn to direct democracy was popularized by observers like J. W. Sullivan, through his widely read and influential report, *Direct Legislation by the Citizenship through the Initiative and Referendum* (1892), and other popular newspaper essays and columns.[76] Sullivan saw direct legislation as rooted in

[76] Steven Piott, *Giving Voters a Voice: The Origins of the Initiative and Referendum in America* (Columbia: University of Missouri Press, 2003), 4-5.

American traditions of town hall democracy, and as a way to bypass the problems of special interest influence and legislative corruption.[77] Sullivan, along with other reformers like Eltweed Pomeroy formed the National Direct Legislation League in 1893, and the *Direct Legislation Record* in 1894, to provide an organizational hub, publicity, and education for state activists seeking to establish direct democratic procedures.[78]

These arguments resonated with the growing reform movement among rural populists, who appealed to direct democracy as a means to temporarily bypass special interest influence in state legislatures to push for substantive reforms favoring farmers, debtors, against workers.[79] While some reformers saw this as a way to achieve true democratic participation and sovereignty, others were motivated less by a desire to promote participation, and more by a desire to create checks on corruption in the hopes of incentivizing more efficient and rational government.[80] These state-level efforts in turn shaped the national political conversation, as the Populist Party endorsed initiative and referendum procedures in its 1896 platform,[81] while Progressive activists in legislatures and governorships helped facilitate the passage of these reforms.[82]

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[77] Piott, *Giving Voters a Voice*, 5-7.

[78] Piott, *Giving Voters a Voice*, 8-9.

[79] Thomas Cronin, *Direct Democracy: The Politics of Initiative, Referendum, and Recall* (Cambridge: Harvard University Press, 1989), 45, 50-58.

[80] Nathaniel Persily, "The Peculiar Geography of Direct Democracy: Why the Initiative, Referendum, and Recall Developed in the American West," *Michigan Law and Policy Review* 2 (1997).

[81] Piott, *Giving Voters a Voice*, 253.

[82] Piott, *Giving Voters a Voice*, 254-5.

Meanwhile, Progressive reformers appealed to majoritarian democracy as a way to bypass the judiciary which had become a conservative barrier to social reform, exemplified not only by cases like *Lochner*, but also through a number of other high-profile rulings that blocked minimum wage laws.[83] These decisions generated heated criticism in the Progressive press, in venues like *The New Republic* and *The Atlantic*, as well as through newspaper columns.[84] Political campaigns against courts as a threat to the democratic majority will became a mainstay of Progressive politics. Teddy Roosevelt made curbing judicial authority a central theme in his 1912 presidential campaign.[85] William Jennings Bryan called for the establishment of national elections for federal judges and proposed recall elections for judges, stripping them of their life tenure.[86] Senator Robert LaFollette proposed a Congressional power to override judicial decisions, later making this a centerpiece of his 1924 campaign for the presidency and his book entitled, *Our Judicial Oligarchy*.[87] Fueled by the legal realist critique of the judiciary as advancing the interests of business through legal formalisms, labor and other reform advocates castigated the judiciary as creating new legal protections for the economic elite.[88]

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[83] See e.g. *Adkins v. Children's Hospital*, 261 U.S. 525 (1923).

[84] Barry Friedman, "The History of the Countermajoritarian Difficulty, Part Three: The Lesson of *Lochner*," *NYU Law Review* 76 (2001), 1383-1455, at 1394-6, 1437-45.

[85] Friedman, "The History of the Countermajoritarian Difficulty," 1444.

[86] Friedman, "The History of the Countermajoritarian Difficulty," 1394.

[87] Friedman, "The History of the Countermajoritarian Difficulty," 1395, 1444.

[88] Friedman, "The History of the Countermajoritarian Difficulty,"1403-28.

In a similar vein, nearly all activists and reformers in this period sought to mobilize citizens through political association as a way to create a more equitable balance of political power. The era was dense with robust, active, and mass membership associations which offered both civic cultivation for their members, as well as a source of countervailing political power to represent the interests of their members in electoral politics. But there was a core ambivalence, though, among reformers over the degree to which such civic mobilization should emphasize conflict between classes and social groups—such as through labor militancy—or instead transcend political conflict to promote conciliatory deliberation among citizens.[89] For example, the government crackdown following the Pullman strike of 1894 split reformers, with some reformers embraced the aggressive conflictual vision of labor strikes, while others including John Dewey and Jane Addams became disenchanted with destructive class antagonisms, seeking ways to shift politics away from such conflict towards more conciliatory and productive reform.[90] Reformers seeking labor legislation often focused on efforts that could draw the support of multiple classes such as social insurance, putting them in conflict with organized labor itself.[91] In other reform debates, Progressives exhibited a similar ambivalence between mobilizing to contest the power of big business and seeking reforms with cross-class appeals to 'good government' in

[89] See e.g., Nancy Rosenblum, *On the Side of Angels: An Appreciation of Parties and Partisanship* (Princeton: Princeton University Press, 2008).

[90] See e.g. Shelton Stromquist, *Reinventing "the People": The Progressive Movement, The Class Problem, and the Origins of Modern Liberalism* (Urbana: University of Illinois Press, 2006), 25-32. See also Louis Menand, *The Metaphysical Club* (New York: Farrar, Straus, and Giroux, 2001), 310-316 (describing the debate between Dewey and Addams over whether the clash of class and social interests as in the labor movement could ever be fully reconciled).

[91] Stromquist, *Reinventing "the People"*, 90-3.

hopes of transcending class conflict, partisanship, and other forms of social conflict.[92]

Forging the regulatory state

These same aspirations to overcoming political blockages, and developing alternative channels for citizens to engage in politics, check elite influence, and address pervasive economic concerns drove efforts to construct the modern administrative and regulatory state. The development of new regulatory agencies staffed by policy experts offered reformers the hope of an effective new tool for managing the increasingly complex modern economy, and asserting the public good against powerful private actors such as trusts or corporations. The regulatory state could be achieved at both the local and national levels through the founding of new commissions and agencies, in both cases sidestepping the problems of political corruption and capture within legislatures.[93] Thus, from 1880 to 1920, the Progressive push to regulate businesses achieved tremendous "innovation in the social control of business, industry, and the market," through "a panoply of new ideas like public utilities, rate regulation, price discrimination, fair rate of return, valuation, just price, and economic planning."[94] This explosion of regulatory activity at both the federal and state level was marked by common techniques of centralization and administrative policymaking and enforcement.[95] These tensions

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[92] Stromquist, *Reinventing "the People", 55.*

[93] See Postel, *The Populist Vision*, 138-9.

[94] William Novak, "Law and the Social Control of American Capitalism," *Emory Law Journal* 60 (2010), 377- 405, at 403.

[95] See generally Novak, "Law and the Social Control."

and struggles to construct such new regulatory institutions are most clearly seen in three parallel policy debates during the period: first in efforts to create public utilities and state oversight of prices in key industries; second in the antitrust movement; and third in early efforts at financial regulatory reform responding to the Panic of 1907 and through the creation of the Federal Reserve Bank itself. In all three of these domains, Progressives experimented with new institutional forms aimed at asserting social control over the economy, but each of these efforts raised deep disagreements between reformers over how to balance the need to check market actors against the need to also ensure the robustness of state institutions to corruption or limiting them from exercising unchecked authority.

Social control through public utilities

Widespread efforts to establish public utilities as a mechanism for regulating industries such as urban transportation, telecommunications, warehouses, banking, and basic commodities constituted a key domain of experimentation with new forms of regulation, but these efforts were constrained by conflicting visions of regulatory goals and structure. The argument for treating formerly private industries as public utilities gained traction both as a response to the activities of the companies themselves, and as an effort to reduce political corruption in legislatures.[96] Thus, urban reformers sought to break the private power of railroads, water companies, and other key industries, eliminating their ability to dominate consumers and curry favor with legislatures by building systems of administrative regulation of these industries. Similarly, rural reformers advocated

[96] Rodgers, *Atlantic Crossings*, 134, 148-9.

the creation of nationalized public utilities to replace the privately owned railroads, and the private provision of banking and credit services. Inspired by the model of the Postal Service, farmers hoped that the creation of a centralized, publicly-run bureaucracy would bypass local power centers, eliminate the corruption of political elites catering to business interests, and provide a check on the activities of these businesses themselves.[97] Progressives construed the idea of public utilities broadly, as a way of establishing public ownership and oversight over a range of industries including water, electricity, gas, railroads, telecommunications, warehouses, ice, banking, and milk.[98] The public utility model thus offered a "vibrant and expansive arena for experimenting with unprecedented governmental control over business, industry, and market."[99]

But the convergence around the idea of the public utility belied deep disagreements about the nature of good government of the public utility approach was meant to promote. Some reformers argued that public utilities should be established in more precise and technically determinable domains of natural monopolies, while others argued on the basis of a broader social vision that drew on ideas of illegitimate profit and advocated full public ownership.[100] Meanwhile, efforts to create public commissions such as urban transit commissions around the turn of the century were often backed by a confusing array of supporters including advocates of more democratic and participatory control over industries, organized

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[97] Postel, *The Populist Vision*, 143-56; Rodgers *Atlantic Crossings*, 335-40.

[98] Novak, "Law and Social Control," 400.

[99] Novak, "Law and Social Control," 399-400.

[100] Rodgers, *Atlantic Crossings*, 140.

labor and the poor, and the business elite who saw opportunities for profitable enterprises licensed by these new commissions and argued for nonpartisan, nondemocratic, and limited government through elite and expert administration.[101] Ultimately, concerns about possible corruption in public ownership led to a compromise consensus around insulated, expert-driven regulatory commissions—an institutional form which then proliferated across municipalities, states, and even the federal government. This institutional approach was seen as the best of both worlds, offering public oversight and private ownership, avoiding the corruption that seemed to come with interest-group democratic politics, and establishing minimum standards of conduct while ensuring returns for private businessmen.[102]

Social control through antitrust

A similar set of tensions and concerns shaped the debates over regulation in the antitrust movement. Here, the central cleavage was between efforts to address the problem of monopolies and oligopolies in industries like rail through decentralization, breaking up these entities into smaller firms, or through centralized oversight by regulatory experts. But disagreement about the purposes of antitrust and consistent conservative pushback through the courts worked to mitigate the more radical proposals.

Early battles over antitrust regulation during this period consisted of efforts to impose state-level rate regulations on railroads, whose increasing concentration and competition often put merchants and farmers at a loss facing higher prices.

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[101] Rodgers, *Atlantic Crossings*, 145-8; 137; 150-1.

[102] Rodgers, *Atlantic Crossings*, 151-5.

Such "Granger" legislation, pioneered by the farmers cooperative union of the Grange in the upper Mississippi, spread across the Midwest in states like Illinois, Iowa, Minnesota, and Wisconsin. In these states, legislation established rate commissions that aimed to combat price gouging, which courts had let slide under common law. While initially supported by the Supreme Court as a legitimate exercise of police power, these rate commissions failed to achieve structural economic change, and as their energy dissipated, the Court itself shifted to hold that railroads were entitled to a fair return on their efforts, undercutting the rate regulation rationale.[103] At the federal level, the early efforts to consolidate support around the creation of a new Interstate Commerce Commission (ICC) failed, leading legislators to propose an institutional model of insulated expert policymakers as a way of defusing the political deadlock around railroad regulation, and creating a system that would not be beholden to any one interest group. But the result was an ICC with a weak mandate, one that was narrowed even further as a hostile Supreme Court narrowly construed ICC authority.[104]

Similar debates over the substantive content and institutional structure of antitrust regulation, driven by anxieties over political capture and economically harmful regulation, served to narrow antitrust initiatives such as the Sherman Act and the Federal Trade Commission (FTC).[105] The antitrust movement argued for the more aggressive use of state power to curtail the threat of concentrated private

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[103] See e.g., Robert Rabin, "Federal Regulation in Historical Perspective" *Stanford Law Review* 38 (1985-6), 1189-1328, at 1197-1215.

[104] Skowronek, *Building a New American State*, 140-160.

[105] See e.g. Sklar, *The Corporate Reconstruction of American Capitalism*; Richard Hofstadter, "What Happened to the Antitrust Movement?", in Earl Cheit, ed., *The Business Establishment* (New York: John Wiley & Sons, 1964), 113-151, at 120.

power in the form of large corporations capable of exploiting workers and moving markets to their own advantage. Reformers during this period shared a common distrust of large trusts like Standard Oil, and financial giants like JP Morgan. These reformers thus shared a common view of the problem of antitrust as primarily a problem of *power*, not consumer welfare: the goal of antitrust reform was to prevent the concentration of economic power by trusts and to enhance individual freedom by protecting against economic—and potentially political—domination.[106] The Sherman Act of 1890 expressed this political view of antitrust, advocating the control of private power through economic decentralization.[107]

Brandeis himself was an ardent supporter of the antitrust movement, seeking to counteract the power of monopolies and corporations by using the state to break them up into smaller, less threatening private actors that no longer posed a threat to freedom, fair competition, and democratic politics. This program of antitrust enforcement was part of a broader view of Brandeis to deploy the powers of the state to enforce a more socially beneficial market system. Brandeis argued for regulation of the economy to ensure a more fair and equitable system of market competition, free of excessive domination of powerful private actors such as trusts. As Brandeis argued, "regulation is essential to the preservation and development of competition, just as it is necessary to the preservation and best development

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[106] Robert Pitofsky, "The Political Content of Antitrust," *University of Pennslyvania Law Review* 127 (1979), 1051.

[107] See David Millon, "The Sherman Act and the Balance of Power," *Southern California Law Review* 61 (1987), 1219-1292, especially 1220 (the Sherman Act was "the dying words of a tradition that aimed to control political power through decentralization of economic power, which in turn was to be achieved through protection of competitive opportunity").

liberty."[108] In this vision of "regulated competition," Brandeis sought to harness the benefits of market competition and innovation, while preventing the rise of concentrated private power in the form of trusts or mega-corporations capable of dominating workers and citizens alike. In addition to antitrust enforcement, this vision of regulated competition also required state intervention to assure things like minimum wages and other 'floors' to prevent deleterious forms of competition or 'races to the bottom.' Thus, the state was crucial not only in preventing such concentrations of power, but also in ensuring the smooth functioning of beneficial forms of market competition.[109]

But disputes arose among reformers over whether such concentrated private power could be better checked by policies that promoted a more decentralized economy and polity—for example, by breaking up large firms, and expanding the power of local and state regulatory bodies—or by creating a new, more powerful centralized national government capable of checking and monitoring the excesses of these large firms. The presidential campaign of 1912 revolved largely around a clash over economic regulatory philosophies, as Theodore Roosevelt argued for federal oversight of trusts on the Massachusetts Model, building on his own prior administration's formation of the US Bureau of Corporations in 1903, while Woodrow Wilson called for a more decentralized approach to breaking up trusts into smaller, less threatening elements. The Wilson administration's final legislation creating the FTC in 1914 took a hybrid approach, but as a result

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[108] Brandeis, "Shall We Abandon the Policy of Competition?" *Case and Comment* (1912), in Fraenkel, ed., *Curse of Bigness*, 104-108, at 104.

[109] [109] See e.g. Gerald Berk, *Louis D. Brandeis and the Making of Regulated Competition, 1900-1932* (New York: Cambridge University Press, 2009).

produced an FTC that lacked clear leadership, mandate, or policy on antitrust matters.[110] Brandeis, a key advisor to Wilson and architect of the FTC, saw it as a clearinghouse of information that would benefit small businesses.[111] Meanwhile the Supreme Court continued to undermine the impact of these new regulatory efforts by interpreting the powers of the FTC narrowly.[112]

Social control in financial regulation

These cross-currents among advocates of the emerging regulatory state can also be seen in efforts to expand the regulation of the financial sector, particularly after the Panic of 1907. Although the Federal government had gradually expanded its role in banking regulation through the National Currency Act of 1863, the National Banking Act of 1864, and the creation of Treasury and the Office of the Comptroller of the Currency (OCC), these recurring financial panics were increasingly seen as revealing failures in the basic regulatory architecture of the financial system, including the lack of a lender of last resort, and scattered policies about bank reserve requirements.[113]

Rural farmers in the Populist movement had already made finance a central concern for their advocacy, seeking greater credit and access to cash and calling for silver-based or greenback fiat currency. The common threads in these reform proposals were first an agreement on the importance of a more scientific and

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[110] Thomas McCraw, *Prophets of Regulation* (Cambridge: Belknap Press, 1984), 80-1, 127.

[111] McCraw, *Prophets of Regulation*, 133-34.

[112] See Rabin, "Federal Regulation in Historical Perspective," 1229-35.

[113] Robert West, *Banking Reform and the Federal Reserve, 1863-1923* (Ithaca: Cornell University Press, 1977), 15, 29.

uniform approach to the regulation of money and finance, and second a hostility to private financial firms, which were seen as unaccountable and capricious, and threatening to the basic welfare of ordinary citizens. This hostility to self-interested private financiers, banks, and middlemen led Populists to call for the public provision of credit through a national system financial regulation and loans.[114] For Progressive activists, this "curse of bigness," as Brandeis famously termed it, could only be righted by various regulations aimed at curbing bankers' excesses and rendering them accountable to Congress and to the democratic public. Thus Brandeis proposed the prohibition of interlocking directorates, arguing that bankers must only serve one master rather than running multiple businesses.[115] He also emphasized the role of publicity in making bankers transparent, empowering investors to punish bad banks and make informed decisions of their own.[116]

Corporate business interests, by contrast, worked to defuse these calls for reform by presenting money and banking as apolitical, developing networks of banking experts who could help manage the new financial economy under the legitimacy of dispassionately promoting the public good.[117] These industry voices defused the call for greater social and democratic control over the banking sector by appealing to the market as a self-regulating system, arguing instead for institutionalizing checks on financial activity through market mechanisms like expanding the numbers and powers of shareholders. The New York Stock

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[114] Postel, *The Populist Vision*, 150-59.

[115] Brandeis, *Other People's Money*, 46-8.

[116] Brandeis, *Other People's Money*, 69.

[117] See Livingston, *Origins of the Federal Reserve System*, especially 228-233.

Exchange, for example, successfully resisted more aggressive calls for nationalization or government oversight by appropriating the language of free markets and public welfare, and arguing that existing market mechanisms such as shareholder rights were sufficient to police the financial system and hold firms accountable.[118]

After the Panic of 1907, proposals for financial regulation through a central bank took on new urgency, pitting defenders of *private* control over the banking system against different attempts to institutionalize public control. Opponents of a central bank feared the concentrated economic power of financial interests, and their concern about greater government oversight was not out of a rejection of the state per se, but rather out of a fear that governmental bodies would be captured by industry. Proponents of a central bank couched their arguments not only in terms of economic necessity, but also presented a central bank as a way to ensure the public's capacity to hold the financial sector accountable through a national, public regulatory body. These debates over the creation of the Federal Reserve thus exemplified the tensions inherent in the Progressive response to the market. In creating new institutions to protect the public good against, reformers struggled to simultaneously check the power of private firms while also ensuring that state actors did not themselves become so powerful as to exceed the ability of the public to hold them in check.

Thus, the 1907 Aldrich Plan proposed a central bank conceived as a cooperative union of banks comprised of representatives from small and large

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[118] Julia Ott, "The Free and Open People's Market: Political Ideology and Retail Brokerage at the New York Stock Exchange, 1913-1933," *Journal of American History* 96:1 (2009), 44-71.

banks.[119] Critics feared this institution would be easily captured by Wall Street financiers.[120] Indeed, the ABA succeeded in eliminating a part of the proposal that would have allowed the president to appoint and remove board members.[121] The Aldrich Bill thus came to stand for a ratification of private industry control of the banking sector—which drove the collapse of support for the bill.[122] After the Democrats regaining control of Congress in 1910 and the presidency in 1912 on a platform flatly opposed to the Aldrich bill, subsequent proposals drafted by Carter Glass and supported by Woodrow Wilson emphasized a more centralized governmental authority over the central bank.[123] While many of the congressional experts involved in the drafting of the bill sought to give control of the system to the member banks themselves, Wilson felt the reform would not be accepted unless it was publicly controlled, ultimately securing presidential appointments for all members of the Federal Reserve Board. Over the course of Congressional negotiations, legislators struggled to strike a balance between assuring the independence of the central bank from both government and bankers, ultimately settling on longer tenure terms for Board members, staggered so that no individual president could appoint all of them. The final Federal Reserve Act of 1913 gave greater insulation as well as more flexibility over monetary policy to the new

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[119] Eugene White, *The Regulation and Reform of the American Banking System, 1900-1929* (Princeton: Princeton University Press, 1983), 93-5.

[120] White, *The Regulation and Reform of the American Banking System*, 93.

[121] Robert West, *Banking Reform and the Federal Reserve, 1863-1923* (Ithaca: Cornell University Press, 1977), 75.

[122] West, *Banking Reform and the Federal Reserve*, 86.

[123] West, *Banking Reform and the Federal Reserve*, 91-112; White, *The Regulation and Reform of the American Banking System*, 95-6.

Federal Reserve.[124] This compromise between direct public control and private control therefore defused the conflict around the central bank: progressive and Populist reformers uneasy with financial interests saw the Act as assuring democratic control over the financial system[125], while business interests uniformly backed the bill, appeased by the insulation of the Federal Reserve Board from party politics, the creation of expert advisory committees to help shape Board policies, and the placing of regional reserve banks under the control of local bankers.[126] The very structure of the Fed thus emerged out of an effort to balance concerns with private financial power on the one hand, and ensuring accountable governmental power on the other.

A conflicted Progressive legacy

In the face of tremendous social upheaval and dramatic new forms of private power, reformers and thinkers during the Progressive and Populist movements mobilized to articulate and help realize an alternative vision for American political economy. These reformers uniformly rejected traditional nineteenth century views of laissez-faire thought, arguing that the dynamics of the new industrial economy—in particular the presence of powerful corporations and deep market instabilities—demanded new political organizations, state institutions, and public policies. In the process, these reformers also realized that to achieve their aspirations of socioeconomic reform, they also had to grapple with the

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[124] West, *Banking Reform and the Federal Reserve*, 113-132.

[125] Postel, *The Populist Vision*, 280-1.

[126] Livingston, *Origins of the Federal Reserve System*, 223.

existing political constraints of late nineteenth century democracy, leading many reformers to direct their energies political mobilization and institutional reform as well.

The Progressive Era therefore suggests several implications for contemporary debates in American political economy. First, debates over economic regulation did not follow the caricature of "more" versus "less" state regulation; rather, the debate between reformers and laissez-faire opponents were a more nuanced contest over *what kinds* of regulation would be most robust to the threat of corruption and the difficulties of making complex and effective policies work. Thus, the laissez-faire critique of the state was both a moral and an institutional one. Reformers had to not only develop a richer conception of power and freedom in a market society; they also had to address head-on the anxieties over political capture, corruption, and responsiveness. Socioeconomic change had to come with a change in political institutions and practices themselves. Thus, progressives also developed a range of institutional innovations in democratic institution-building such as expanding political associations, local-level policy experimentation, and democratic engagement with the emerging regulatory state.

Second, later generations of reformers—including the chief architects of economic regulation in the New Deal and the later twentieth century—inherited this Progressive Era critique of laissez-faire understandings of the economy, in particular the concerns over concentrated private power and market instabilities. These concerns drove future reformers to continue their attempts to build the powers of the modern state to promote the public good. But despite a common focus on socioeconomic change and unregulated power, different wings of reformers focused on different—and often conflicting—political institutional

strategies such as anti-monopoly, community mobilization, or regulatory expertise.[127] The unresolved debate among Progressive Era reformers over *what form* such expanded state powers should take—democratic or technocratic; oriented towards mobilized contest between groups or towards expert knowledge and consensus; local or national—created an uncertainty as to what particular vision of politics and state would emerge in future decades.

There remained a troubling ambiguity as to whether these agencies were to be new sites of democratic politics freed from the problems of unequal political power and political capture, or whether they were to be apolitical policymaking entities, separated from politics altogether. Some reformers sought the creation of powerful, elite and expert driven regulatory agencies that could govern modern society efficiently, separated from the vagaries of both democracy and politics itself. Others saw this turn to administration and expertise as a way of narrowing rather than expanding the scope of state action, as administrative agencies would be more prone to fiscal discipline and more minimal state intervention where it is absolutely necessary. Still others saw the regulatory state as a prerequisite and catalyst for a more vibrant, participatory democratic politics. Meanwhile, the hostility that economic regulatory efforts provoked often led reformers to settle upon more conservative regulations and more expert driven institutional forms as a palliative response. For a time, these wings of reform discourse fed one another: emerging faith in expertise and new regulatory bodies seemed compatible with and important bulwarks for the progressive vision of a reformed economic and

[127] Rodgers, "In Search of Progressivism," 123-127.

democratic order. It was only later that tensions between the appeal to expertise and the appeal to democracy began to surface.

The debates of the Progressive Era were enormously influential in shaping American society. Many of the New Deal policies were in fact developed out of inherited Progressive ideas such as antitrust, social insurance, and the regulatory state.[128] But this inheritance also bequeathed an ambivalence over how exactly the state ought to respond to these problems in market society. The ferment of this period put into place *multiple* progressive traditions of economic governance as a response to the dangers of laissez-faire. Once specific policies of economic regulation and the very idea of expert-driven regulatory agencies came under increasing attack from the 1970s as socially harmful and politically corruptible, later progressives found themselves ill-equipped to respond.[129]

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[128] See e.g. Ellis Hawley, *The New Deal and the Problem of Monopoly: A Study in Economic Ambivalence* (New York: Fordham University Press, 1995); Rodgers *Atlantic Crossings*, 413-15.

[129] See e.g. Jodi Short, "Coercive State Anxiety and the Rise of Self-Regulation" (2009), Working paper on file with author; S. M. Amadae, *Rationalizing Capitalist Democracy: The Cold War Origins of Rational Choice Liberalism* (Chicago: University of Chicago Press, 2003); K. Sabeel Rahman, "Conceptualizing the Economic Role of the State: Laissez-Faire, Technocracy, and the Democratic Alternative," *Polity* 43:2 (2011), 264-286.

4 ANXIETIES OF EXPERTISE

Faced with economic upheaval and constrained by the straightjackets of laissez-faire thought and political constraint, Progressive Era reformers and thinkers struggled to develop alternative ways of understanding and governing the new economy. No single settled framework emerged from this period of ferment. There were deep disagreements between those who saw the answer in political and economic decentralization and those who sought a more centralized national state and economy; between those who appealed to the reconciliation between social factions, and those who emphasized political conflict and contest; and between those who valorized new social scientific expertise as the key to regulatory policymaking, and those who instead vested their hopes in the direct participation of citizens themselves. The common thread throughout these diverse understandings of politics and the economy was the struggle to establish some form of social control over the economy. The disagreements arose over what institutional framework and core political values would animate this reassertion of collective agency over the new industrial economy.

It was out of this Progressive intellectual inheritance that the policymakers and thinkers of the New Deal developed their own response to the calamity of the Great Depression. In many respects, the New Deal represented the culmination and realization of Progressive Era aspirations, finally establishing a range of powerful national regulatory agencies to promote the interests of consumers and labor, and to check the excesses of finance and powerful corporations—all in the name of the

democratic public that had empowered the Roosevelt administration and its allies in Congress. In the process, the New Deal changed the fabric of American political economy—and the nature of the debate over economic governance.

The New Deal consolidated a conceptual framework of technocratic economic governance, which emphasized the role of neutral, insulated expert regulators managing the economy, as a truer servant of the democratic public than traditional branches of government. By the 1940s, the diversity of democratic thought and institutional innovation that marked the Progressive Era response to laissez-faire had been replaced by the ascendancy of this technocratic vision. As a result, the Progressive Era discourse of economic governance shifted in three important ways. First, it preferred insulated expert-led regulatory agencies rather than the democratic public as the driver of economic regulation. Second, it took the purpose of such regulation to be not a fundamental restructuring of the modern economy, but rather the facilitation and optimization of the market itself. Finally, this view shifted the understanding of citizens from active participants in government to consumers in the economy.

It was this vision of market-optimizing, technocratic regulation that formed the dominant intellectual paradigm that later twentieth century thinkers and policymakers would challenge—and that contemporary progressives like Obama would later seek to emulate. As laissez-faire critiques of economic regulation revived in the late twentieth century, defenders of this New Deal legacy responded by doubling down on and subduing this technocratic approach. By then the more radical democratic tradition of economic governance had been largely forgotten. The limits of this thinner, constrained technocratic vision helps explain the

difficulties of contemporary efforts to expand regulation in the aftermath of the financial crisis.

Progressivism realized—and transformed

After his election in 1932, Franklin Roosevelt and his New Deal agenda drew much of their moral force and initial policy ideas from the Progressive arguments of previous decades.[1] While Roosevelt's early New Deal is often seen as a period of policy innovation—almost to a fault, as contemporaries and later commentators would criticize Roosevelt for implementing scattershot policies with little overarching vision—many of the ideas themselves were inherited from the earlier ferment of the Progressive Era. As historian Daniel Rogers argues,

> The paradox of crisis politics is that at the moment when the conventional wisdom unravels, just when new programmatic ideas are most urgently needed, novel ones are hardest to find. The need for well formulated solutions goes hand-in-hand with conditions least suited for reflective policy formulation: haste, confusion, the opportunism of expediency, the impossibility of perspective on the onrushing events. One of the most important aspect of crises, in consequence, is that they ratchet up the value of policy ideas that are waiting in the wings, already formed though not yet politically enactable.[2]

The crisis of the Great Depression altered the "conditions of the politically possible," and suddenly a host of policy ideas developed during the Progressive Era

[1] Daniel Rodgers, *Atlantic Crossings: Social Politics in a Progressive Age* (Cambridge: Harvard University Press, 1998), 413-5; Otis Graham, *An Encore for Reform: The Old Progressives and the New Deal* (New York: Oxford University Press 1967), 6-8.

[2] Rodgers, *Atlantic Crossings*, 414.

seemed both attractive and politically feasible in a way that they had not during the 1920s.[3]

FDR openly embraced much of the rhetoric of Progressive Era reformers who castigated the concentrated power of large firms as a threat to the economy and to the ideals of political liberty. In one famous 1932 speech in Columbus, Ohio, for example, Roosevelt attacked the Hoover administration for being enthralled to the business elite. Like Hoover, FDR proclaimed his support for American individualism but he argued that Hoover's deeds contributed to the demise of such individualism by encouraging the concentration of economic power in a few elite institutions. "I believe that the individual should have full liberty of action to make the most of himself," Roosevelt declared. "But I do not believe that in the name of that sacred word a few powerful interests should be permitted to make industrial cannon fodder of the lives of half the population of the United States."[4] Roosevelt blamed "the ruthless manipulation of professional gamblers" for the stock market crash.[5] In opposition to these elite interests, Roosevelt argued for the expansion of government authority as a crucial check acting on behalf of a democratic public:

> I believe that the Government, without becoming a prying bureaucracy, can act as a check or counterbalance to this oligarchy so as to secure the chance to work and the safety of savings to men and women, rather than safety of exploitation to the exploiter, safety of manipulation to the financial manipulators, safety of unlicensed power to those who would speculate to the bitter end with the welfare and property of other people.[6]

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[3] Rodgers, *Atlantic Crossings*, 413.

[4] Franklin Delano Roosevelt, Campaign Address at Columbus Ohio, August 20, 1932.

[5] Roosevelt, Address at Columbus, Ohio.

[6] Roosevelt, Address at Columbus, Ohio.

Throughout the 1930s, Roosevelt continued to assert this central theme defending the importance of government to promoting the interests of the democratic public. Even the frontiersmen of the eighteenth century turned to government as a mechanism through which individuals could cooperate to improve their welfare and pursue their goals:

> Government was an indispensible instrument of their daily lives, of the security of their women and their children and their homes and their opportunities. They looked on government not as a thing apart—as a power over our people. They regarded it as a power of the people, as a democratic expression of organized self-help.[7]

Americans struggling with the Depression, FDR argued, must view government as an "ally," as evidenced by New Deal programs to insure bank deposits, provide mortgage support, protect against foreclosure, and develop social insurance. Such aggressive governmental action was necessary to promote the common good—but for Roosevelt, it was also important to view this government action as subject to the will of the democratic public. "Let us never forget," he argued, "that government is ourselves and not an alien power over us. The ultimate rulers of our democracy are not a President and Senators and Congressmen and Government officials but the voters of this country."[8]

This familiar Progressive-style rhetoric was backed by major policy successes, particularly in financial regulation. Financial reform was one area where New Dealers hearkened back to more traditional arguments of the sort associated with Louis Brandeis that regulation was needed to constrain the concentration of

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[7] Franklin Delano Roosevelt, Address at Marietta, July 8, 1938.

[8] Roosevelt, Address at Marietta.

power in the financial sector.[9] Roosevelt was deeply influenced by Progressive Era writings on the subject, especially Brandeis' tract *Other People's Money*, and was sympathetic with the Progressive and Populist effort to create aggressive federal regulations that would supersede lax state level oversight of financial and securities firms—who had proven adept in lobbying state legislatures.[10] Immediately after taking office, FDR signed the Emergency Banking Act of 1933, which in addition to providing for an immediate bank holiday to stem the tide of bank runs, for the first time provided explicit support for governmental backing of deposits as a key way of promoting confidence in the banking system. The Roosevelt administration also passed a series of other financial reform statutes including the 1933 Banking Act, and the Securities Act, the 1934 Securities Exchange, and the Banking Act of 1935.

The regulatory efforts of the early New Deal thus viewed business "not as a power to be propitiated or, at the very least, as a partner to be cajoled, but as an erratic and irresponsible force requiring strict social discipline."[11] Unlike other New Dealers who believed in the power of big institutions in business and in government to generate social welfare and who sought to set up a national economic planning apparatus, those who were behind financial reform lacked such "faith…in the virtues of bigness and of industrial self-government, and propos[ed] instead to use the federal power to revitalize and police the competitive economy."

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[9] Ellis Hawley, *The New Deal and the Problem of Monopoly: A Study in Economic Ambivalence* (Princeton: Princeton University Press, 1966), 306.

[10] Joel Seligman, *The Transformation of Wall Street: A History of the Securities and Exchange Commission and Modern Corporate Finance* (Boston: Northeastern University Press, 1995), 40-43.

[11] Arthur Schlesinger, *The Crisis of the Old Order 1919-1933* (Boston: Houghton Mifflin, 1957), 444.

Collectively, these statutes expressed Roosevelt's vision of establishing regulatory oversight of financial firms and monopolies.

These policies established a stable and well-regulated financial sector that persisted for several decades by creating a governmental backstop for depositories and establishing tight structural limits on the powers of financial companies, and the scope of future financial innovation. Thus the creation of the Federal Deposit Insurance Corporation (FDIC) and deposit insurance led to a dramatic decline of bank failures played the financial system prior to the 1930s. New Deal legislation also enabled the Federal Reserve to set ceilings on savings account interest rates (Regulation Q) while separating investment and commercial banking provisions such as the Glass-Steagall Act, incorporated into the 1933 Banking Act. As a result, "postwar commercial banking became similar to a regulated utility, enjoying moderate profits with little risk and low competition."[12] Further, by separating different types of financial industries like investment and commercial banks, mortgage lenders, and finance companies from one another, the New Deal regulatory framework compartmentalized the economic activities of different financial firms, and "fragment[ed] the financial sector into diverse industry groups that found it difficult to cohere around a unified political agenda."[13] In the 1970s, the financial sector composed just over 3 percent of US GDP, with pay comparable to the rest of the private sector. This system of "boring banking"—a system that lacked the complex array of wildly profitable and risky securities that marked the

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[12] Simon Johnson and James Kwak, *13 Bankers: The Wall Street Takeover and the Next Financial Meltdown* (New York: Vintage, 2011), 35.

[13] Greta Krippner, *Capitalizing on Crisis: The Political Origins of the Rise of Finance* (Cambridge: Harvard University Press, 2011), 61.

pre-2008 crisis economy—proved more than adequate to facilitate postwar economic growth and relatively high incomes for workers in the financial sector.[14]

These statutes also went a long way towards establishing the importance of public oversight of the financial sector, articulating a vision of government that was more than just an optimizer of market functioning, but rather was an aggressive promoter of the public welfare by establishing near public ownership or public guarantees of vital social necessities such as the currency, banking deposits, credit, and utilities.[15] Indeed, the fault lines during these debates were more often between proponents of the bills and Progressives who wanted even more radical centralization and government control over the financial sector. Older Progressives in Congress largely supported the Roosevelt administration's efforts as realizing the aspirations of the Progressive Era, more often criticizing the administration for not going far enough rather than expressing outright opposition.[16]

But by the end of the New Deal, this Progressive vision had been dramatically transformed in three ways: first, shifting from democratic to technocratic institutions of governance; second, by subduing the substantive goals of regulation to one of optimizing the market; and third, by viewing citizens not as agents in governing but as consumers.

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[14] Johnson and Kwak, *13 Bankers*, 61-4.

[15] See Ronnie Phillips, *The Chicago Plan and New Deal Banking Reform* (Armonk: ME Sharpe, 1995), 115-134.

[16] See generally Graham, *Encore for Reform*; Phillips, *The Chicago Plan*, 42-4.

From democracy to technocracy

New Dealers gradually pulled away from the more participatory and democratic visions that animated earlier generations of Progressive reformers. Where several early New Deal efforts at economic planning involved a heavily participatory structure including direct citizen involvement in the planning process, through local advisory boards, and engaged civic participation,[17] over time these efforts eroded.[18] As historian Alan Brinkley notes, late New Dealers in particular sought to achieve familiar economic goals such as regulation of monopolies through resort to more centralized technocratic policymaking rather than decentralized and participatory democratic alternatives. These New Dealers were thus "coming to a common vision of government—a vision of capable, committed administrators who would seize control of state institutions, invigorate them, expand their powers when necessary, and make them permanent actors in the workings of the marketplace."[19]

This specifically technocratic vision was perhaps most forcefully articulated by one of the central architects of the New Deal, James Landis. Speaking at Yale University in 1938, Landis gave what remains one of the most assertive defenses of the emerging administrative and regulatory state. A protégé of Felix Frankfurter, a former clerk of Supreme Court Justice Louis Brandeis, and a leading young law professor, Landis was already celebrated as one of drivers of the creation of a new

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[17] See James Kloppenberg, "Deliberative Democracy and Poverty in America," in *Virtues of Liberalism* (New York: Oxford University Press, 1998), 106-8.

[18] See e.g. David Ciepley, *Liberalism in the Shadow of Totalitarianism* (Cambridge: Harvard University Press, 2006), 98-115.

[19] Alan Brinkley, "The Late New Deal and the Idea of the State," in *Liberalism and Its Discontents* (Cambridge: Harvard University Press, 1998), 37-62, at 44-45.

financial regulatory institution, the Securities and Exchange Commission (SEC), which he would later chair.

As Landis argued, these new regulatory agencies responded to both the challenges of the modern industrial economy, and the "inadequacy" of traditional institutions of governance.[20] The creation of this new governmental power was a necessary "response... to the demand that government assume responsibility not merely to maintain at the levels in the economic relations of the members of society, but to provide for the efficient functioning of the economic processes of the state."[21] Such economic mastery could only come through the use of regulatory agencies, staffed by specialized experts capable of making policy on the substantive merits rather than according to the dictates of interest group politics or the archaic limits of legal doctrine. Landis was dismissive of both Congress and the courts as institutions incapable of fully responding to modern needs in a complex and rapidly changing economy. Agencies could make more effective public policy by drawing on specialized expertise, and could do so more rapidly than legislatures or courts. "The administrative process is, in essence," wrote Landis, "our generation's answer to the inadequacy of the judicial and legislative process."[22]

Not only were agencies superior; they also required a free hand in order to act effectively. "It is easier to plot away through a labyrinth of detail," proclaimed the Landis, "when it is done in the comparative quiet of a conference room than when it is attempted amid the turmoil of the legislative chamber or a committee

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[20] James Landis, *The Administrative Process* (New Haven: Yale University Press, 1938), 1.

[21] Landis, *The Administrative Process*, 16.

[22] Landis, *The Administrative Process*, 46.

room."[23] Expertise was thus vital to developing public policies that would actually promote the common good and be effective in light of the complex modern economy. But to harness the benefits of such expertise, policies needed to be crafted by regulatory agencies that, although created by Congress and overseen by the judiciary and the elected executive, enjoyed broad delegations of power and relative independence.[24] Indeed, rather than restraining agencies through narrow grants of power and tight oversight, Landis preferred to give agencies a relatively free hand, relying instead on the beneficial effects of publicity of agency policies and their justifications,[25] as well as the professionalism, expertise, and independence of agencies[26] to ensure that they served the common good.

This technocratic vision was institutionalized through the formation and consolidation of regulatory agencies. The early New Deal faced several stiff legal challenges to efforts to create new regulatory agencies—most famously, the Supreme Court unanimously struck down Roosevelt's National Industrial Recovery Act for delegating unconstitutionally broad powers to executive agencies in the name of coordinated economic planning[27]—and the legal community continued to express anxieties about the constitutional status and potential or arbitrary or authoritarian power on the part of regulatory agencies. But by the late

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[23] Landis, *The Administrative Process*, 70.

[24] Landis, *The Administrative Process*, 55.

[25] Landis, *The Administrative Process*, 62.

[26] Landis, *The Administrative Process*, 99-100.

[27] *A.L.A. Schechter Poultry Corp. v. United States*, 295 U.S. 495 (1935).

1930s the Landis-style theory of insulated regulatory expertise had been effectively endorsed by the Supreme Court.[28]

From contesting power to managing the market

While the New Deal consolidated a shift from citizens to experts as the drivers of economic policy, it also shifted the substantive goals of such economic regulation. In practice, many of the New Deal policies themselves proved to be less aggressive, and more market-friendly than earlier Progressive Era thinkers may have envisioned. By mid-century, the kind of aggressive oversight and checks on economic power that animated earlier generations of reformers like the antitrusters would give way to a more managerial and market-friendly view of the purposes of economic regulation.

The example of the Securities and Exchange Commission (SEC) is instructive. From the outset, the Securities and Exchange Acts of 1933 and 1934, which collectively established the SEC, proved in practice to be a more tentative and ultimately market-friendly construction of Progressive Era reform ideals. The malfeasance of financial firms and securities dealers was one area where Progressive Era critiques of financial firms' power to manipulate prices and outright fraud had taken root as the primary political narrative of the crisis, and the main motivation for the reforms themselves, particularly after the Pecora

[28] See e.g. Mark Tushnet, "Administrative Law in the 1930s: The Supreme Court's Accommodation of Progressive Legal Theory," *Duke Law Journal* 60 (2011), 1565-1639, at 1569-75; Reuel E. Schiller, "The Era of Deference: Courts, Expertise, and the Emergence of New Deal Administrative Law," *Michigan Law Review* 106:3 (2007), 399-441, at 413-35; Robert Rabin, "Federal Regulation in Historical Perspective," *Stanford Law Review* 38 (1985-6), 1189-1328, at 1254-61.

hearings in Congress.[29] But the SEC itself was formed essentially as a compromise, as financial sector lobbying led to the creation of a separate regulatory agency, rather than conveying the power to regulate securities to the already-established Federal Trade Commission (FTC)—a move that the financial sector as well as opponents of the bill saw as a weakening of the reform proposal.[30] The business lobby, including the National Association of Manufacturers and the Chamber of Commerce, even succeeded in resisting the nationalization of stock exchanges; the 1934 Securities Exchange Act left the New York Stock Exchange as a private, self-regulatory organization.[31]

Once established, the early leaders of the SEC like James Landis and William Douglas sought to combine Progressive ideals of economic regulation with their faith in social science and expertise.[32] But rather than employing the emphasis of Progressive Era democrats like Brandeis on self-rule and participation, the SEC focused on the goals of economic efficiency, investor protections, and smoothing the functioning of the market.[33] In place of the more democratic visions of Progressive Era reformers, the SEC instead cast itself as "a site for the production and application of economic knowledge."[34] The SEC also committed early in its

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[29] See Seligman, *Transformation of Wall Street*, 12-36.

[30] Seligman, *Transformation of Wall Street*, 70, 97.

[31] Ott, "Free and Open People's Market," 71.

[32] Jessica Wang, "Imagining the Administrative State: Legal Pragmatism, Securities Regulation, and New Deal Liberalism," *Journal of Policy History* 17:3 (2005), 257-293, at 260-62.

[33] Jessica Wang, "Neo-Brandeisianism and the New Deal: Adolf A. Berle, Jr., William O. Douglas, and the Problem of Corporate Finance in the 1930s," *Seattle University Law Review* 33 (2010), 1221-1349, at 1222.

[34] Wang, "Imagining the Administrative State", 265; See also Wang, "Neo-Brandeisianism and the New Deal," 1222.

existence to a strategy of regulation via third-party industries, for example by creating incentives for accountants, self-regulating exchanges, and financial professionals themselves to police each other.[35] While this approach may have magnified the enforcement capacities of the SEC for a time, they also worked to blunt the more radical reformist potential of the SEC.

Thus the SEC focused its actual enforcement efforts on relatively noncontroversial activities such as the maintaining of disclosure requirements and accounting standards, narrowly interpreting its regulatory authority in an effort to maintain its legitimacy and avoid interfering with the profitability of financial firms.[36] The operative language of § 10 of the Act, for example,[37] empowered the SEC to prescribe rules that would make it unlawful for financial firms to employ any manipulative or deceptive practices when devising or advertising financial instruments. The SEC—and later the judiciary, following several legal challenges to the new agency's powers—interpreted this section to mean that the SEC was empowered primarily to compel financial firms to disclose the terms of their

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[35] Thomas McCraw, "With Consent of the Governed: SEC's Formative Years," *Journal of Policy Analysis and Management*, 1:3 (1982), 346-70.

[36] Seligman, *Transformation of Wall Street*, 349-50, 568.

[37] Securities and Exchange Act, §10 (1934): "It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or any facility of any national securities exchange—(a) to effect a short sale…(b) to use or employ…any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors." This statutory text was implemented by the SEC in Rule 10(b)-5, 13 FR 8183 (Dec 22, 1948), as amended by 16 FR 7928, Aug 11, 1951: "It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange: (a) to employ any device, scheme, or artifice to defraud, (b) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statement made, in light of the circumstances under which they are made, not misleading, or (c) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security."

financial instruments. Yet this focus on disclosure was only a part of the original reformist vision animating the 1934 Act, which envisioned a robustly empowered SEC that would require disclosure but also do much more to prevent the manipulation of stock prices.[38]

Even for signature New Deal financial regulatory statutes, like the Glass-Steagall Act and the separation of investment and commercial banking, repackaged older Progressive and Populist concerns in a new language of technocratic macroeconomic management, where the problem was not one of a moral economic vision or democratic accountability of finance, but rather of economic efficiency and enhancing economic growth.[39] This represents the second key shift from the discourse and ethic of earlier Progressive reformers: not only moving from a focus on democratic empowerment and mobilization to an emphasis on expertise, but also a tempering of the substantive goals of economic regulation itself, focusing not on the accountability of private power but rather on promoting macroeconomic growth and efficiency.

Most New Dealers saw this shift as a pragmatic response to the realities of a complex economy. Despite Roosevelt's own campaign rhetoric, the New Deal brain trust as a whole was largely dismissive of Progressive Era appeals to democratic accountability and the threat of concentrated private power. For example, Raymond Moley, one of FDR's main advisors on antitrust and financial regulation policy, saw big business as a key to promoting productivity, growth,

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[38] See Steve Thel, "The Original Conception of Section 10(b) of the Securities and Exchange Act, *Stanford Law Review*, 42:2 (1990), 385-464.

[39] See K. Sabeel Rahman, "Democracy and Productivity: The Glass-Steagall Act and the Shifting Discourse of Financial Regulation," *Journal of Policy History*, 24:4 (2012), 612-643.

and higher standards of living, seeking to turn away "from the nostalgic philosophy of the trust busters."[40]

In part out of a fear that more aggressive economic regulation could be a pathway towards the kind of totalitarianism increasingly on view in Europe during and after World War II,[41] New Dealers searched for more neutral and broadly acceptable foundations for the legitimacy of state policy.[42] This shift to economic policy as compensation—for example, through welfare spending—represented an effort to ground the growing economic role of the state on a relatively uncontroversial vision of economic progress.[43] Especially after World War II, policymakers had less enthusiasm for the earlier Progressive vision of powerful state regulation, instead shifting to this ideal of compensatory government where the state would use fiscal policy to facilitate growth without directly getting involved in the oversight, planning, and coordination of industries.[44] This reconceptualization of the goals of regulation gradually alienated the older generation of Progressives who increasingly clashed with FDR.[45] The development of these ideas of economic regulation during the late 1930s and 1940s is thus "the

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[40] Raymond Moley quoted in Seligman, *Transformation of Wall Street*, 40.

[41] See Ciepley, *Liberalism in the Shadow of Totalitarianism*.

[42] See generally, Michael Sandel, *Democracy's Discontent: America in Search of a Public Philosophy* (Cambridge: Harvard University Press, 1998).

[43] See e.g. Ciepley, *Liberalism in the Shadow of Totalitarianism*, 81-98; 146-63; Sandel, *Democracy's Discontents*, 250-74.

[44] See Brinkley, "The Late New Deal," 53-62.

[45] See e.g. Graham, *An Encore for Reform*.

story of a slow repudiation" of earlier Progressive Era commitments, and "the elevation of other hopes to replace them."[46]

From citizens to consumers

Just as the late New Deal inaugurated a shift to a vision of government not as a tool for fundamental economic restructuring and regulation, but rather as a mode of compensation for the vagaries of an otherwise acceptable market economy, this period also saw a shift in understandings of how best to meet the needs of ordinary citizens themselves. Where earlier Progressive Era thinkers had often emphasized the importance of empowering workers and consumers as a political force to check the excesses of corporations, by the late New Deal era, these understandings had been supplanted by a less overtly politicized idea of the consumer. Thus, early New Deal efforts adopted the Progressive Era view of the consumer as citizen, where empowering consumer groups would promote the public good by enabling them to contest government and corporate actions to improve consumer rights, safety, and market fairness.[47] For example, the National Recovery Act, the Agricultural Adjustment Act, and the Tennessee Valley Authority all incorporated representatives of consumer interests alongside those of business and labor within the governing structures of these bodies. Meanwhile, other agencies like the FDIC and the SEC sought to incorporate consumer interests

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[46] Brinkley, "The Late New Deal," 62.

[47] Lizabeth Cohen, *A Consumer's Republic: The Politics of Mass Consumption in Postwar America* (New York: Alfred Knopf, 2003), 18-28.

into their policies even if they lacked procedures for consulting consumer groups directly.[48]

Indeed, although this Progressive vision of a politicized identity of the consumer as a form of countervailing power capable of pressuring corporations and the state remained central for postwar thinkers like John Kenneth Galbraith, the late New Deal moved instead to a vision of the consumer not as a matter of empowerment and representation, but rather as a way to boost economic demand and output, thus expanding growth and promoting the public interest without undermining the basic system of capitalism.[49] 'Consumers' went from a political identity asserting rights against big business to a vague framework for promoting economic activity. Continued efforts at financial regulation increasingly shifted their focus on promoting disclosure, as a way of better optimizing activities of buyers within the market—rather than creating direct and political forms of citizen empowerment.

Consumer interest programs were gradually dismantled by 1950s, while businesses themselves started to claim the mantle of looking out for consumer interests. The very idea of the consumer thus gradually became depoliticized: it was no longer a defined segment of society to be empowered as countervailing power, but rather as a shorthand category that encompassed everyone and no one, a group whose interests amounted to getting value for their purchasing dollars,

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[48] Cohen, *A Consumer's Republic*, 28.

[49] Cohen, *A Consumer's Republic*, 24.

rather than having defined rights and powers as against the interests of corporations, or the state.[50]

The New Deal thus consolidated and realized, but also narrowed, the aspirations of Progressive Era reformers. It succeeded in establishing powerful regulatory agencies with a broad mandate to manage the modern market economy at the scale envisioned by earlier reformers battling ideas of laissez-faire and the upheavals of the new industrial economy. At its height, this technocratic vision offered the promise of a solution to the Progressive dilemma: it provided a way to address the dangers of the modern market economy, through institutions that could themselves claim to be pursuing the public good free of the dangers of political corruption and special interest influence that, for laissez-faire critics and Progressive activists alike, afflicted traditional political processes of elections, parties, and legislation.

But in so doing, the New Deal also shifted the terms of Progressive imagination in three ways: from a focus on democratic mobilization to an emphasis on technocratic expertise; from a focus on policies aimed at contesting private power and fundamentally reshape the workings of the market to policies that sought instead to simply manage and optimize the market; and finally from viewing citizens as political and economic agents to be empowered, to instead viewing them as consumers. These altered understandings sowed the seeds of this technocratic vision's own demise, for it made the argument for economic regulation against laissez-faire critics rest on the basic contention that expert regulators could better satisfy the needs of consumers and optimize the functioning

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[50] Cohen, *A Consumer's Republic*, 129-132.

of the market. As this faith in expertise declined in the late twentieth century, these same goals of market optimization and consumer welfare seemed to be better met through deregulation and the free market. With the more moralized and aggressive overtones of democratic action to contest economic power left behind, the technocratic vision had few intellectual resources left to combat this resurgence of laissez-faire thought.

Laissez-faire revived, technocracy chastened

The erosion of the technocratic vision accelerated in the late twentieth century in the face of a renewed fear of economic regulation by the state motivated by Cold War politics, the rise of public choice theory, and the mobilization of conservative intellectuals aimed at rolling back the New Deal. This assault prompted efforts to shore up the legitimacy of technocratic economic governance through the growth of administrative law and procedural constraints on regulation. It also prompted the growing trend towards deregulation especially in the 1980s and 1990s. To the extent that the technocratic vision survived the assault, it did so by retreating to an even more minimalist and chastened form, through institutional reforms aimed at maximizing regulatory expertise, and through increasingly market-friendly approaches to economic regulation.

A renewed fear of the state

This basic concern of expansive regulation through administrative agencies as a threat to liberty magnified in the postwar era, particularly as American thinkers and policymakers sought to differentiate themselves from the specter of

totalitarian politics in fascist and communist Europe. These concerns combined with another intellectual trend to fuel a resurgence of laissez-faire thought in the late twentieth century: the rise of market based models of politics, and public choice theory. Where nineteenth century laissez-faire thought rejected state regulation out of a fear of legislative capture and corruption, this revived laissez-faire critique focused the same arguments against the regulatory institutions inherited from the New Deal.

The concerns about totalitarianism and liberty forced emerging disciplines of social science to confront the tension between their search for objectivity on the one hand, and their commitment to the moral ideals of democracy on the other—a tension which had been largely overlooked during the Progressive Era. In the aftermath of the Depression and the New Deal, economists and political scientists searched for the value-free social science, leading to gradual emergence of public choice theory as the new mainstream conceptual framework for understanding the politics of the regulatory state. The result was a new science of politics that expressed deep skepticism about the possibilities of democratic governance and public interested regulation.[51]

Public choice theory rested on an initial critique of the irrationality of collective choices. The Nobel laureate Kenneth Arrow authored landmark series of studies in the 1940s which showed that there was no single way to aggregate diverse individual preferences into a rational collective preference. Although Arrow saw this critique relevant to both collective decisions made by the market and by

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[51] Edward A. Purcell, Jr., *The Crisis of Democratic Theory: Scientific Naturalism and the Problem of Value* (Kentucky: University Press of Kentucky, 1967), 46; S. M. Amadae, *Rationalizing Capitalist Democracy: The Cold War Origins of Rational Choice Liberalism* (Chicago: University of Chicago Press, 2003), 88-102.

the state, most economists presumed that the decentralized system of the market which matched individual preferences with goods and services precluded the need for collective rationality in the first place. As a result, Arrow's theoretical critique was taken more as an argument against the rationality of collective democratic politics and state-driven public policy.[52]

Arrow's findings sparked a rich intellectual current of scholarship which over subsequent decades eroded faith and the very idea of effective democratic politics. First, public choice theorists like James Buchanan and Gordon Tullock of the University of Virginia built on Arrow's findings to recast politics as a marketplace for self-interested parties maximize their individual utilities, leading to transactions between policymakers seeking support and interest groups seeking favorable treatment from the state.[53] This kind of political transaction created a skepticism of the very idea of the common good as the illusory at best, or legitimizer for state tyranny at worst.[54] Second, another wave of theorists built on these findings to argue that the democratic public itself was irrational: either because it was cost-effective for individual voters to remain ignorant or uninvolved in the political process, or because this ignorance and demobilization magnified the likelihood that special interests would successfully "capture" state institutions, using them to further their own private interests rather than the public good.[55]

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[52] Amadae, *Rationalizing Capitalist Democracy*, 106-17.

[53] Amadae, *Rationalizing Capitalist Democracy*, 133-55.

[54] Amadae, *Rationalizing Capitalist Democracy*, 172-5.

[55] Amadae, *Rationalizing Capitalist Democracy*, 176-89. See also Jessica Leight, "Public Choice: A Critical Reassessment," in Edward Balleisen and David Moss, eds., *Government and Markets: Toward a New Theory of Regulation* (New York: Cambridge University Press, 2009).

These intellectual currents established the ideas of free-riding, rent-seeking, and interest group capture as mainstays of the social science and broader public discourse. The public interest, according to these views, was illusory, and governmental failure endemic. The natural implication seemed to suggest that the public good could ironically be best served by deregulating large segments of the economy, removing the danger of interest or capture altogether.[56] This theory of political power as a matter of economistic and self-interested transactions supplanted rival theories of collective and cultural power. In contrast to the left's growing focus on culture and consciousness as domains of power, or the previous generation of social scientists who examined the power of institutional, economic, and political structures, this economistic notion of power seemed more objective, simple, and tractable.[57] Indeed, public choice theory purported to be more than conjecture; it also appeared to have empirical backing through case studies of governmental corruption and capture.[58] Although many of these empirical foundations were themselves shaky as a matter of scholarship,[59] the overall intellectual framework proved persuasive. As Edward Purcell notes, in this new science of politics, "objectivism and skepticism concerning democracy went together," as public choice theories and their empirical foundations "appeared to

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[56] Daniel Rodgers, *Age of Fracture* (Cambridge: Belknap Press, 2011), 86-9.

[57] Rogers, *Age of Fracture*, 98.

[58] Leight, "Public Choice"; David Moss and Mary Oey, "The Paranoid Style in the Study of American Politics," in Balleisen and Moss, eds., *Government and Markets*.

[59] *Ibid*.

confirm the arguments of those who claimed popular government did not and could not work."[60]

Business interests and conservative philanthropists helped bankroll and gradually popularize these revived laissez-faire critiques.[61] By focusing not on electoral politics, but rather on the production of ideas, policy analysis, and public intellectuals, this growing conservative movement helped build the intellectual foundations for the deregulatory turn.[62] As one historian notes, "the think tanks, radio stations, magazines, and intellectual organizations that were funded by business contributions during the 1950s helped to form the infrastructure for the rise of the conservative movement." From Hayek's Mont Pelerin Society to the conservative journals like the *National Review*, and to more scholarly institutions like the Olin Foundation and the Heritage Foundation, "all of these organizations relied on the contribution of businessmen, and all of them sought to encourage businessmen to do what they could to fight the power" of the New Deal state, and its primary political constituents including labor unions.[63] With these conceptual foundations in place, the conservative movement could shift to more explicit policy advocacy, through organizations like the Chamber of Commerce which by the 1970s commenced a systematic lobbying effort aimed at promoting deregulation in defense of the "free enterprise system".[64]

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[60] Purcell, *Crisis of Democratic Theory*, 109.

[61] Rogers, *Age of Fracture*, 47-76; Kim Phillips-Fein, *Invisible Hands: The Making of the Conservative Movement from the New Deal to Reagan* (New York: WW Norton, 2009), 13-19.

[62] Phillips-Fein, *Invisible Hands*, 42-56.

[63] Phillips-Fein, *Invisible Hands*, 86.

[64] Phillips-Fein, *Invisible Hands*, 160-5.

The political implications of this conceptual shift seemed clear: in place of the muscular faith of New Dealers in the capacity of expert regulators to promote the public good, postwar social science seemed to suggest—scientifically, no less—that regulation was instead highly suspect, prone to capture, and inefficiency. Landis himself, by 1960 when he authored a special report on regulatory reform for the White House, saw the regulatory state as broken by inefficiency and threatened by the risk of interest group capture.[65] Combined with a concerted political challenge by business interests on the New Deal state,[66] this forced defenders of the idea of economic regulation to engage in successive waves of reform aimed at defusing these growing anxieties about the power of the emerging regulatory state. Scholars of the regulatory state became increasingly skeptical of the desirability of New Deal-style regulation, further influencing the thought and practice of judges, policymakers, and practitioners.[67]

In response, defenders of the regulatory state tempered their aspirations further in three ways: developing legal procedural constraints on the exercise of regulatory authority; dismantling those institutions through deregulation; and by pursuing a more chastened form of economic regulation focusing on market-friendly policies.

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[65] Thomas McCraw, *Prophets of Regulation* (Cambridge: Belknap Press, 1984), 217-19.

[66] See e.g. Phillips-Fein, *Invisible Hands*.

[67] See e.g. Jodi Short, "The Paranoid Style in Regulatory Reform," Georgetown Public Law and Legal Theory Research Paper No. 11-10 (2011).

Restraining technocracy through procedure

One response to this growing unease with regulatory authority was to restrain regulatory agencies through legal procedures.[68]

From the very beginning, the New Deal expansions of regulatory authority were met by stiff opposition, particularly from the legal elite. The earliest debates pitted unapologetic defenders of the authority of expert regulators by New Dealers like James Landis—who saw scientific expertise and bureaucratic professionalism as sufficient guarantors of publicly-spirited regulation[69]—against legalists like Roscoe Pound and the American Bar Association who feared the reach of regulatory institutions that existed apart from the constitutional schema of separated adjudicatory, legislative, and executive functions—and therefore seemed to pose a threat for unaccountable and illiberal state power.[70] The Supreme Court initially struck down one of FDR's centerpiece New Deal programs, the National Industrial Recovery Act, which authorized the executive branch to approve codes of conduct and production set up by industries themselves. The Court saw this as

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[68] This historical account is by now familiar in the administrative law literature. See e.g. Elena Kagan, "Presidential Administration," *Harvard Law Review* 114 (2001), 2245-2385, at 2253-4; Stewart, "The Reformation of American Administrative Law"; Gerald Frug, "The Ideology of Bureaucracy in American Law," *Harvard Law Review* 97 (1983-4), 1276-1388; Morton Horwitz, *The Transformation of American Law, 1870-1960* (New York: Oxford University Press, 1992); Reuel Schiller, "Enlarging the Administrative Polity: Administrative Law and the Changing Definition of Pluralism, 1945-1970," *Vanderbilt Law Review* 53:5 (2000), 1390-1453; Reuel E. Schiller, "The Era of Deference: Courts, Expertise, and the Emergence of New Deal Administrative Law," *Michigan Law Review* 106:3 (Dec 2007), 399-441; Peter Strauss, "From Expertise to Politics: The Transformation of American Rulemaking," *Wake Forest Law Review* 31 (1996), 488-526; Robert Rabin, "Federal Regulation in Historical Perspective," *Stanford Law Review* 38 (1985-6), 1189-1328.

[69] See e.g. Landis, *The Administrative Process*.

[70] See Horwitz, *Transformations 1870-1960*, 217-240 (recounting a famous debate between James Landis and Roscoe Pound over the legitimacy of modern regulatory agencies).

an unconstitutional delegation of legislative authority to the executive branch, striking down the act in *A. L. A. Schechter Poultry Corp. v. United States*.[71]

These concerns gave rise to the 1946 Administrative Procedure Act (APA). The legislative debate around the APA revolved around this central concern over preventing unchecked agency action and the risk of special interest influence and corruption. Prior to the APA's passage, supporters of the more strict Walter-Logan bill saw tougher procedural constraints on agency adjudication and rulemaking as necessary to resist a drift into totalitarianism,[72] while Roosevelt saw such strict procedures as actually undermining the power of the administrative state to pursue the public interest against the concentrated power of special-interest groups.[73] The APA represented a turn to legalism as a reaction against the powers of the administrative state, seeking to constrain agencies not by the professional ethic of objective, neutral expertise, but rather through legal procedures.[74] As Morton Horwitz notes, "every triumph of proceduralism occurred at the expense of professionalism."[75]

Nevertheless, these initial skirmishes in the immediate post-New Deal era left agencies with relatively broad powers; Congress could of course establish new constraints as well as new directives by legislation, but by and large the New Deal

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[71] *A.L.A. Schechter Poultry Corp. v. United States*, 295 U.S. 495 (1935) (invalidating the National Industrial Recovery Act, holding that "Congress is not permitted to abdicate or to transfer to others the essential legislative functions with which it is vested.")

[72] See Walter Gellhorn, "The Administrative Procedure Act: The Beginnings," *Virginia Law Review* 72:2 (1986), 219-233.

[73] Horwitz, *Transformations 1870-1960*, 232.

[74] Horwitz, *Transformations 1870-1960*, 231-3.

[75] Horwitz, *Transformations 1870-1960*, 235.

faith in administrative expertise had won out. The APA provided some minimal constraints but left agencies with much room to develop their policies. But as the scope of regulatory authority expanded in the 1960s and 1970s with broad delegations of authority on matters such as air and water quality, environmental protection, and consumer safety,[76] so too did concerns about agency accountability and especially the risks of special interest capture of regulatory agencies.

In light of declining faith in agency expertise and neutrality, courts and legislators began to shape exercise of agency discretion to require agencies to give adequate representation to the range of affected interests, through revised judicial doctrines of due process,[77] standing,[78] and through statutory participation rights.[79] This attempt to expand the diversity of interests represented within agency policymaking was a direct response to the growing concerns about agency capture—and the growing skepticism that any one institution could identify and represent the common good as Landis and the New Deal architects envisioned.[80] Courts temporarily became key guarantors of fair and balanced interest representation within regulatory agencies, less inclined to defer to agencies, and employing tougher doctrines of review.[81] This framework of interest representation backed by judicial oversight responded to the problem of capture

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[76] See e.g. Rabin, "Federal Regulation in Historical Perspective," 1279-91.

[77] Stewart, "Reformation of American Administrative Law," 1717-22; Schiller, "Enlarging the Administrative Polity," 1428-35.

[78] Stewart, "Reformation of American Administrative Law," 1723-47; Schiller, "Enlarging the Administrative Polity," 1435-43.

[79] Stewart, "Reformation of American Administrative Law," 1748-56.

[80] Schiller, "Enlarging the Administrative Polity," 1398-1414.

[81] Schiller, "Enlarging the Administrative Polity," 1415-28.

and disparate political power.[82] Alongside this renewed judicial oversight of agencies, Congress instituted statutory provisions to enable greater transparency and accountability of agencies in the 1960s. The Freedom of Information Act made agency deliberations more readily transparent to the public, while citizen suit provisions in statutes like the Clean Air Act made it easier for citizens to challenge agency decisions in court.[83] Similarly, Johnson's War on Poverty created statutory requirements that anti-poverty programs experiment with "maximum feasible participation" when developing and implementing policies.[84]

But these efforts were relatively short-lived. The more aggressive expansions of interest representation and participation through judicial review and statutory schemes like the War on Poverty were soon curtailed, after much controversy. Even defenders of such expanded interest representation came to view it as a flawed policy, making regulation even more gridlocked and controversial without necessarily yielding better policies.[85]

Deregulation

A second response to growing fears of the regulatory state was to simply dismantle it. This view grew particularly in the 1980s, following the retreat from

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[82] See e.g. Thomas Merrill, "Capture Theory and the Courts: 1967-1983," *Chicago-Kent Law Review* 72 (1996-7), 1039-1117 (arguing that judicial review in the 1960s and 1970s worked to push agencies to expand representation and participation of stakeholder interests in shaping regulatory policies). See generally Stewart, "The Reformation of American Administrative Law," 1713-56; Schiller, "Enlarging the Administrative Polity,"1415-43.

[83] Schiller, "Enlarging the Administrative Polity," 1444-50.

[84] Rabin, "Federal Regulation in Historical Perspective," 1272-4.

[85] Stewart, "Reformation of American Administrative Law," 1776-82.

efforts to thicken administrative procedures, and as the renewed laissez-faire critique became more mainstream. This return to market-based mechanisms was partly the result of the persuasiveness of public choice theory, and market-based ideals of freedom. In contrast to the corruption, inefficiency, and illiberalism of technocratic regulation, markets seem to offer an ideal of freedom, choice, and reason. Furthermore, as self-equilibriating systems, they seemed more effective and adaptable to a complex modern economy.[86]

This deregulatory turn is well-exemplified in the politics of financial regulation, where regulatory agencies and policymakers themselves became the leaders of the deregulatory turn, resulting in a boom in the financial sector. The provisions of the Glass-Steagall Act, for example, had already been largely eviscerated through regulatory policy changes and court rulings even before the formal repeal of the provision in 1999.[87] Formally, Glass-Steagall prohibited national and state banks from purchasing and selling securities except for treasuries, also prohibiting affiliates that were "principally engaged" in securities activities. The terms of the statute left room for agencies to interpret these requirements, and as early as the 1960s, the Office of the Comptroller of the Currency (OCC) attempted to relax the requirements of the Act, only to be prevented by judicial rulings against such a shift. But by 1989, renewed agency efforts to deregulate were being upheld by courts.[88] The SEC also took a cautious approach to its activities during the 1980s and 1990s, while constantly facing

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[86] Rogers, *Age of Fracture*, 42.

[87] George Kaufman and Larry Mote, "Glass-Steagall: Repeal by Regulatory and Judicial Reinterpretation," *Banking Law Journal* 107 (1990), 388-421.

[88] Kaufman and Mote, "Glass-Steagall," 407-8.

budgetary pressure from Congress with little support from either Republican or Democratic administrations on policy initiatives or appointments.[89] The SEC increasingly failed to engage in enforcement of existing rules, its powers sapped by budget cuts and a growing 'revolving door' culture of interchange between regulators and financial firms.[90]

These various deregulatory measures played a direct role in driving the boom of subprime lending, foreclosures, mortgage-backed derivatives, short term commercial paper markets, and other contributors to what eventually became the 2008 financial crisis.[91] Under Alan Greenspan, the Fed declined to regulate the range of new financial products and securities that have emerged out of the deregulatory financial sector boom.[92] Similarly, regulations on derivatives gradually eroded from the 1980s onwards, first by the overseeing agency, the Commodity Futures Trading Commission (CFTC) issuing exemptions for swaps and declining to regulate derivatives, and then codified by the 2000 Commodity Futures Modernization Act of 2000 exempted derivatives from restrictions, leading to an explosion of derivatives trading.[93] Perhaps most glaringly, the SEC issued a ruling that exempted the largest investment banks from minimum capital

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[89] Seligman, *Transformation of Wall Street*, 577, 639, 743.

[90] Norman Poser, "Why the SEC Failed: Regulators Against Regulation," *Brook Journal of Corporate Finance and Commercial Law* 3 (2008), 289-324, at 317-21.

[91] Timothy Canova, "Financial Market Failure as a Crisis in the Rule of Law: From Market Fundamentalism to a New Keynesian Regulatory Model" *Harvard Law and Policy Review* 3 (2009), 369-396, at 374-77; Simon Johnson and James Kwak, *13 Bankers: The Wall Street Takeover and the Next Financial Meltdown* (New York: Vintage, 2011), 64-86.

[92] Johnson and Kwak, *13 Bankers*, 89

[93] Lynn Stout, "Derivatives and the Legal Origin of the 2008 Crisis," *Harvard Business Law Review* 1 (2011), 1-38.

requirements, permitting these companies to engage in self-regulation with minimal SEC monitoring—a move that seemed to contribute significantly to the boom in the kinds of complex and risky mortgage-backed securities that were at the heart of the 2008 crisis, and which freed the hands of the major firms Bear Stears, Merrill Lynch, Morgan Stanley, and Lehman Brothers, nearly all of which are now defunct or absorbed by other firms following their collapses in 2008-9.[94]

This return to 'free markets' was backed by an increasingly popular ideology of finance. In academic circles, innovations in theoretical economics led to conceptual frameworks such as the efficient markets hypothesis, which argued that well functioning financial markets would optimally price assets according to risk, and therefore allocate social resources most effectively. These academic accounts combined with the growing profitability of the financial sector to help drive a new generation of financial markets advocates and practitioners.[95] The increasing economic sway of the financial industry also helped spread this ideology of finance throughout political discourse. In addition to direct political lobbying through campaign contributions an interest group politics, the financial sector was also able to create an environment where policymakers increasingly shared the same worldview and preferences as the industry itself, convinced that what was good for the financial sector will ultimately be good for the broader economy as a whole. Key policymakers like Alan Greenspan at the Fed and liberals such as Robert Rubin in the Clinton administration's Treasury Department presided over but

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[94] Poser, "Why the SEC Failed," 296; Vanessa Drucker, "SEC Killed Wall Street On April 28 2004," *Real Clear Markets*, February 19, 2009; Stephen Labaton, "Agency's '04 Rule Let Banks Pile Up New Debt, and Risk," *New York Times*, October 3, 2008.

[95] See e.g. Justin Fox, *The Myth of the Rational Market: A History of Risk, Reward, and Delusion on Wall Street* (New York: Harper Business, 2011).

continued deregulation and expansion of the financial sector, convinced that this approach would ultimately promote economic growth and social welfare.[96]

In a triumph for the laissez-faire view, financial markets gradually came to be seen not only as an acceptable feature of the modern economy, but also as an attractive policy tool with which to promote economic efficiency, consumer welfare, and growth, further relegating the more radical and moralized visions of financial regulation into the background. By deregulating the financial sector, expanding credit for borrowers, and emphasizing consumption driven prosperity for all, policymakers were able to win the support of both consumer activist groups and business lobbies, while avoiding more explicit value judgments over the allocation of scarce social resources. Thus, "policymakers' reliance on market mechanisms did not plunge the state into divisive conflicts about how to allocate limited resources, … but rather allowed policymakers to dissolve emerging political tensions into what for the moment appeared to be a return to prosperity."[97] This allure of political neutrality not only helped drive the financialization of the economy and set the stage for the run-up to the 2008 crash; it also animated a broader shift in political discourse away from substantive questions of the good economy towards a more neutral focus on maximizing economic growth.

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[96] See Johnson and Kwak, *13 Bankers*, 90-119.

[97] Greta Krippner, *Capitalizing on Crisis: The Political Origins of the Rise of Finance* (Cambridge: Harvard University Press, 2011), 141.

Technocracy redux

In the face of this deregulatory onslaught, defenders of economic regulation reformulated their own ideals, attempting to absorb and thereby defuse the revived laissez-faire critique. Thus, even defenders of the regulatory state after the 1980s began to speak in terms of minimizing the costs of regulation, of narrowing the purpose of state action to closing market failures, and of employing greater cooperative measures between regulation on the one hand and more efficient and less coercive market mechanisms on the other.

This "new Chicago School" of regulation shared with the old Chicago school of Milton Friedman an awareness of the social and economic costs of regulation, but sought to rescue the technocratic ideal of welfare-enhancing public policy by developing new tools for expert regulators themselves.[98] Regulators themselves thus increasingly turned to measures such as cost-benefit analysis to provide objective proof and legitimation for the social value of regulations,[99] while reforming regulatory policies themselves to allow for more deregulation, market-based regulation, and self-regulation where possible.[100] This new vision of regulation would make it more efficient, flexible, and cost-effective.[101]

In effect, these efforts to constrain agencies to prevent corruption, capture, and ineffectiveness have ironically resulted in a regime that increasingly relies once again on the professionalism and expertise of the regulators themselves. The

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[98] Lawrence Lessig, "The New Chicago School," *Journal of Legal Studies*, 27:2 (1998), 661-691.

[99] See e.g., Short, "The Paranoid Style in Regulatory Reform," 10.

[100] See e.g. Short, "The Paranoid Style in Regulatory Reform," 23-29.

[101] Short, "The Paranoid Style in Regulatory Reform," 35.

rationality, professionalism, and expertise of regulators seems to protect against the dangers of interest group capture, and ensure effective policymaking.[102] As Sheila Jasanoff writes, where earlier 1960s and 1970s efforts to reform regulation appealed to public participation, this more contemporary turn indicates a return to the ideal of expertise.[103] This response to the laissez-faire critique thus ironically reconstituted the New Deal appeal to expertise and technocracy, but it was a different vision of technocracy than the one espoused by Landis and early New Dealers. In place of their confidence in regulatory expertise and mastery, these new defenders of regulation appealed to the value of *appropriately-constrained* expertise—expertise bound by the requirements of cost-benefit analysis, transparency, and ultimately oversight by the democratically-elected Executive.

Defenders of economic regulation thus absorbed the critique leveled by resurgent laissez-faire thought, moving towards a more minimalist, market-friendly approach to economic regulation—a more chastised regulatory state, in contrast to the kind of aggressive vision of early New Deal architects like Landis.

A turn to democratic theory

With the revived laissez-faire critique of the regulatory state we come back full circle to where this Part began, with the Obama era efforts to respond to the 2008 financial crisis. The trajectory of ideas of economic governance—from aggressive New Deal regulation that harnessed technocracy to pursue Progressive

[102] Martin Shapiro, *Who Guards the Guardians? Judicial Control of Administration* (Athens: University of Georgia Press, 1988), 14-15.

[103] Sheila Jasanoff, "Constitutional Moments in Governing Science and Technology," *Science Engineering Ethics* 17 (2011), 621-38, at 632

Era reform visions, to a more chastised regulatory state that preserved its commitment to technocracy but increasingly took a more market-friendly approach to policy in an attempt to stave off controversy and anxiety over regulatory power—helps explain how the financial regulatory system inherited by Obama had become one that combined both unaccountable technocratic governance and increasingly market-friendly policies.

The policy response to the 2008 crisis follows the recent tradition of managerial and technocratic regulation as outlined in this chapter, appealing to technocratic oversight, with relatively limited structural impositions on too-big-to-fail firms, while still facing ongoing concerns about the exercise of technocratic authority. This technocratic vision presents itself as the solution to the problems of the market: regulatory agencies possess the expertise and authority to correct the failures and mitigate the harms of market society, while their very expertise and insulation from ordinary democratic politics bind them to promoting only the public good. But this approach is particularly problematic for, as Chapter 3 outlined, the central force of the laissez-faire critique is the concern of corruption and capture on the one hand, and an appeal to markets as more effective social institutions for promoting the public good free of such corruption on the other. It is the revived version of this critique that helped animate efforts to dismantle the New Deal state, and continues to bedevil efforts to expand and reform economic regulation today. The end result of these critiques was to create a more technocratic and chastened regulatory state, one that absorbed the laissez-faire celebration of markets, and which saw the role of the state in terms of the minimalist deployment of expertise to manage and optimize the market order.

But the technocratic approach to economic governance is not the only way to deliver on the critique of laissez-faire that animated Progressive Era thinkers, and which seems even more relevant today after the 2008 crisis. As these last two chapters suggest, early twentieth century critics of the market generated a much wider array of ideas, institutions, and aspirations than those that remain after the consolidation and erosion of the technocratic vision over the rest of the twentieth century. Indeed, this critique of the market can lead alternatively to a more aggressive approach to responding to the exercise of private and market power, through a democratically participatory, responsive, and accountable institutional channel than the technocratic managerial approach. This democratic alternative appeals to the political engagement of citizens themselves to drive checks on both markets and expert agencies. The democratic tradition of participatory Progressive Era thinkers like Dewey and Brandeis offers some starting points for a revived democratic vision of economic governance. Articulating this vision is the task of Part II.

PART II

5 ECONOMIC GOVERNANCE AS A PROBLEM OF AGENCY

The mainstream response to the 2008 financial crisis followed the New Deal-inspired playbook. In the face of market failure and economic upheaval, reformers turned to the promise of insulated, expert regulators to manage financial markets. But this was not the only way to understand or respond to the financial crisis. A more radical group of reformers argued for a very different approach. Instead of focusing on the more limited goal of mitigating market failures, these reformers argued for more structural changes in an economy that had become too dominated by finance. Instead of pursuing these policies through expert oversight, these reformers also saw a greater role for public mobilization and structural limits on the size and capacities of financial firms. As with the pre-New Deal Populists and Progressives, these radical voices in 2009-2010 saw economic governance not as a matter of technical management of the market, but as partly a moral problem raised by the economic power of finance, and partly a political problem of disparity of influence between industry and ordinary citizens.

This tension among reformers suggests the potential of an alternative, more democratic approach to economic governance. But the weakness of this alternative reform vision in practice speaks to its relatively emaciated form in contemporary political discourse. We are familiar with the claim to self-optimizing markets or to expert oversight, but these more moralized, democratic arguments for strict limits on financial firms and a greater role for citizen mobilization raise skepticism.

These next three chapters outline a normative account of democratic economic governance that can ground such reform alternatives.

This chapter argues that the problem of economic governance should be understood not as a technical matter of policy design to be addressed through scientific expertise, but rather as a fundamentally *moral* problem of power. First, there is the problem of private power, where individual actors or firms exercise undue influence over the wellbeing of individuals and society by virtue of their command over economic and political resources. Second, there is the problem of market power, where the aggregate system of market exchange creates dynamics that unduly constrain individual or collective opportunities. Both of these types of power threaten a core moral value of agency—the capacity of individuals and groups to author their own lives. Recasting economic governance as a project of protecting agency against private and market power suggests a very different motivation for political action than the approach presumed by technocratic views of economic governance. The turn to politics, in this more moralized account, is motivated out of a desire to secure the agency of citizens against private and systematic threats. While this may involve complex policy responses, it is a fundamentally different motivation than the technocratic notion of optimizing market functioning.

This focus on the moral value of agency also suggests a framework for shaping the exercise of state power to respond to the moral threats of the market. The ideal of agency suggests that there is a legitimate moral critique of technocratic regulation. Even if the regulatory state addresses the moral problems of the market, it poses its own threat to agency if such actions are too distanced from our own roles as democratic citizens. For critics of the market, then, there is an

additional challenge of structuring our response to the problems of private and market power in ways that express, rather than displace or undermine, citizen political agency.

The market as a threat to agency

As outlined in Part I above, the technocratic view of economic governance built on critiques of the market by harnessing the capacities of neutral expertise to promote the public good. But this technocratic turn represents only one possible manifestation of the rich criticisms of laissez-faire developed during that pre-New Deal period of economic upheaval. From legal realist thinkers like Morris Cohen and Roger Hale to jurists like Louis Brandeis and philosophers like John Dewey, these Progressive Era thinkers developed a sophisticated critique of market society that still carries force today. Drawing from these thinkers, a common theme emerges: the problem of the market is not fully captured by economistic concepts such as "market failure." Rather, the most pressing moral challenge of the market is in its threat to the *agency* of individual citizens, groups, and the polity as a whole. Market actors and aggregate market forces can undermine the individual's agency to live a meaningful life; at the same time, these actors and forces defy the abilities of the individuals and groups affected to contest and check these constraints on their agency. Specifically, these threats take two forms: the problem of concentrated private power such as that of large corporations, and the problem of systematic market power, where the aggregate dynamics of market forces constrain the agency of individuals and groups.

Private power

Whether in the form of highly influential economic elite such as hedge fund managers or powerful "too-big-to-fail" firms like Lehman Brothers, there are a number of entities who possess the power to impact a wide range of economic actors, through their direct impact on the economy, as well as through their abilities to leverage this economic power into political influence on public policy. Yet these actors are accountable to only a very small subset of those who are potentially affected by their actions. Nor do these private entities arise out of a 'natural' process of achieving efficient economic production; the powers and capacities of these firms are themselves a product of a legal regime that has often been influenced to favor firm interests.[1]

This threat of concentrated private power can take a number of forms. The most familiar threat arises from the danger that elites of this kind can dominate those in less powerful positions beneath them. Within the firm, owners and managers possess disproportionate authority over the livelihood, wellbeing, and life opportunities of workers within the firm. The hierarchical structure of most corporations create "islands of command" within the 'free' market,[2] as the experience of most workers within the workplace is very much one of subjection to managerial authority.[3] This "arena of authority and control" of managers over workers within the firm belies the laissez-faire defense of the market as a domain

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[1] See generally, William Roy, *Socializing Capital: The Rise of the Large Industrial Corporation in America* (Princeton: Princeton University Press, 1997); Charles Perrow, *Organizing America: Wealth, Power, and the Origins of Corporate Capitalism* (Princeton: Princeton University Press, 2002). See also David Ciepley, "Beyond Public and Private: Toward a Political Theory of the Corporation," *American Political Science Review* 107:1 (2013), 139-158.

[2] Charles Lindblom, *The Market System* (New Haven: Yale University Press, 2002), 78.

[3] Lindblom, *The Market System*, 184-5.

of free exchange that generates greater freedom, productivity, and social progress.[4] These forms of power in market society have long since informed turns to regulation in an effort to mitigate such unchecked authority over workers, for example through regulations protecting labor standards and shareholder rights.

Such private power also creates repercussions for those outside the immediate authority of corporate managers or owners. In a market society, entities that command greater wealth can exercise indirect control over the flow of money, goods, and opportunities in society—for example, by shaping market prices, influencing other buyers and sellers, or leveraging their wealth for political and social advantage.[5] While capitalism as a system is premised on competition, the modern economic landscape does not match the ideal of small firms in a competitive market; rather, many industries are marked with large, powerful firms that have high concentrations of wealth and power within the industry. These are precisely the kinds of concerns that animated Progressive Era antitrust activists; in contrast to contemporary anti-trust discourses, these reformers sought to curtail concentrated economic power not in the name of consumer welfare and lower prices for goods. Monopoly pricing was noted, but it was not the main offense; it was, rather, a symptom of the power exercised by big firms over the well-being of citizens who had no control over the decisions of these firms.[6]

There is another related manifestation of private power, where large firms or highly wealthy individuals leverage their economic wealth to influence the

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[4] See David Ciepley, "Authority in the Firm (And the Attempt to Theorize it Away)," *Critical Review* 16:1 (2004), 81-115, at 83.

[5] Lindblom, *The Market System*, 63-4.

[6] See for example, the arguments of Louis Brandeis, described in Chapter 3.

political process, skewing public policy to favor their interests over the general public. This is part of the concern arising in context of large firms from the Standard Oil monopoly of the nineteenth century to the threat of too-big-to-fail (TBTF) banks today. The problem here is not one of direct or indirect economic power, but rather the degree to which economic power is translated into political power and influence. This concern manifests, for example, in debates over lobbying influence, revolving door policies for state officials, and campaign finance reform efforts. This influence can take the form of both direct pressure, as well as more subtle forms of cultural, ideological, or prestige-based influence.

In all of these cases, the core problem is that a particular set of private actors have, by virtue of their accumulated wealth, the capacity to dominate others in society whether directly, indirectly, or through their capture of the policy process. The problem, in other words, is the lack of sufficiently powerful channels through which citizens can contest the exercise of power by the economic elite. The remedy to this problem may involve familiar mechanisms of redistribution or social insurance but the root of the problem is not just a matter of disparate economic resources; it is one of disparate power.

Today this concern with private domination by concentrated economic interests is relatively underemphasized. In the prevailing technocratic understanding of economic policy, these concerns are understood in more narrow economistic terms, robbed of their political-emancipatory potential. For example, to the extent that anti-trust efforts exist today, they focus more narrowly on unfair pricing and competitive practices. In the financial crisis, the problem of TBTF banks has been predominantly understood in terms of the economic costs that such firms might impose through the risk of their potential collapse. But TBTF is

arguably better understood as a problem of political and economic domination threatened by such concentrations of economic influence.

Market power

Distinct from the concentrated power of private actors, there is another threat to agency that arises from the aggregate system of the market. This threat arises in two mechanisms.

First, although markets nominally allow voluntary choice, market exchanges are in fact structured coercive interactions, depending on the differential bargaining power of conflicting groups—buyers and sellers, employers and labor. Where differences in bargaining position are too great, market outcomes can be exploitative. This critique was forcefully made by legal realist thinkers as described in Chapter 3 above.

Second, markets create a more indirect form of *decentralized* or *diffused* coercion, where systematic and structural effects arise from the aggregation of individual transactions that impose a constraint on individual freedom and well-being. Unlike the problem of private power, the impact on others here arises from no single blameworthy actor, but rather from the aggregation of actions under existing incentive and rules. Market power points to the ways in which the decentralized system of market transactions aggregates into market forces that narrow the choice set of individuals, particularly when arising against a background condition of economic inequality. These market forces are socially constructed—they can be reshaped and channeled in different ways depending on the background structure of private law of contract, property, torts, and through state regulation. But to each individual, these forces seem exogenous, seemingly

natural order, against which individuals must optimize or to which they must adapt.

This more diffuse form of "market power" can manifest in different ways. Markets can be thought of as coercive in that they condition freely-chosen benefits on meeting unrelated conditions which themselves are harmful to the chooser.[7] Markets may also be seen as coercive in that free choices provide people with better outcomes than the otherwise would have enjoyed, but these outcomes remain below what might be considered normatively preferable. For example, choosing to sell one's labor may make the worker better off by providing more income, but if the wages are insufficient, then the worker's well-being while improved remains below a moral baseline. Finally, markets can be seen as systems which narrow our choice sets in the first place. Thus, while the actual choice may be voluntary, a choice between two unsavory options is hardly meaningful freedom. Viewed in this way, markets need to be supplemented by an expansion of individual capabilities and agency. "The fact that these evils [of suffering in market society] are the product of voluntary choices hardly justifies them: free choice within a set of options does not justify the set of options itself," argues Elizabeth Anderson. "The primary subject of justice is the institutional arrangements that generate people's opportunities over time."[8] Further, "people's real or hypothetical market choices offer no guidance whatsoever to what citizens are obligated to provide to one another on a collective basis."[9]

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[7] David Grewal, *Network Power* (New Haven: Yale University Press, 2008).

[8] Elizabeth Anderson, "What is the Point of Equality?" *Ethics* 109:2 (1999), 287-337, at 308-9.

[9] Anderson, "What is the Point of Equality?" 309-310. See also John Dewey, *Liberalism and Social Action* (New York: Prometheus, 2000), 54.

Consider an individual job-seeker in a highly competitive market. To cut costs, firms will necessarily seek to reduce labor costs by offering lower wages, creating a “race to the bottom” as wage levels drop. The decline in wages is the product of human action, aggregated across firms and participants in the market for that particular good. But in the aggregate, it is experienced as an exogenous constraint on the job-seeker: of all the jobs she can seek, the wage levels remain too low to provide sufficient basic income. To the extent that other essential goods for living such as food, healthcare, and the like, are also subject to market forces of supply and demand, the constraint experienced from declining wages magnifies the vulnerability of the job-seeker in these other markets where her ability to acquire the necessary goods for life is dependent on her wage income.

The financial crisis offers another telling example. The crisis itself arose from a combination of subprime lending, securitization, and risky financial innovations like credit default swaps that created a highly instable system of financial risk with harmful effects for many workers, homeowners, and pensioners. Although there certainly was widespread fraud and abuse, this system arose not through any one actor’s malfeasance but rather through the aggregated impact of individually rational and legal decisions. The systemic nature of the financial crisis captures a broader feature of market society: markets clearly have an effect on individual capacities, options, and choices, but these constraints arise from a combination of disparities in bargaining power between individual parties to a market transaction and aggregate effects of otherwise unintentional or legitimate transactions. At the same time, such diffuse systemic market forces are largely immune to contestation or check: while we are all harmed by systemic financial risk, very few of us have the economic or political resources to influence every

individual actor who contributed to the entire system of securitization, lending, and systemic risk.

Thus, unlike paradigmatic cases of state tyranny or monopolistic malfeasance, markets are defined by patterns of behavior in which no single actor is responsible, but where the aggregation of thousands of transactions can create a systemic force that poses a very real threat to individual freedoms. In this way, a diffused and decentralized system such as the market can nevertheless constrain individual freedom and agency—whether by creating risks for economic collapse, or, for example, low wages through "race to the bottom" competition for cheap labor. Such structural or systemic power represents another form of domination, albeit one that arises from a diffused and decentralized system.

Politics as a response to private and market power

Viewing the market economy as a moral problem of power suggests that our response must expand the capacities of individuals and groups who are affected to contest and challenge such exercises of power. Private power and market power constrain the agency of individuals to live meaningful lives, subjecting them to the direct effects of powerful entities like large corporations or to the indirect and aggregate effects of market forces. But these threats are magnified because individuals *as individuals* lack the capacities to contest or challenge these imposed constraints.

The most pernicious moral threat of the market is therefore the way in which it undermines the very concept of political agency. The market as a concept seems to remove these kinds of problems of private and market power outside the

realm of politics and human agency. We refer to "market forces" and "the market" as a monolithic entity that decides things like prices or wages in the manner of akin to the forces of nature, the weather, or the turning of the planets.[10] The very decentralized nature of market society that makes it difficult to justify economic regulations, for they appear as unduly coercive constraints on an otherwise seemingly free market system.[11] But as noted by Progressive critics of the market explored in Chapter 3, the market is not simply a natural system, but rather a product of background policies, laws, and distributions of power and wealth. These background conditions are themselves a result of political decisions, and are not necessarily morally perfect or socially optimal. The veneer of market freedom obscures realities of power, intimidation, coercion, and manipulation.[12] The market as a concept constrains the realm of political and conceptual

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[10] See Karl Polanyi, *The Great Transformation* (Boston: Beacon Books, 2001). As Polanyi notes, laissez-faire rests on a view that the economy is governed by 'natural' laws beyond the scope of human agency. Such a conceptualization of economic order implies "no less than the running of society as an adjunct to the market" (60). It is this mindset that can undermine efforts to promote economic welfare and poverty-reduction policies. "The true significance of the tormenting problem of poverty now stood revealed," argues Polanyi. "Economic society was subject to laws which were *not* human laws" (131).

[11] See e.g., Friedrich von Hayek, "Social or Distributive Justice", in Chiaki Nishiyama and Kurt Leube, eds., *The Essence of Hayek* (Stanford: Hoover Institution Press, 1984), 62-99. The decentralized nature of market society makes it difficult to justify decommodifying intervention and welfare state provisions against the charge that such policies represent undue coercion and interference with individual freedom. Hayek himself tellingly refutes such claims of social justice precisely on the grounds that there is no identifiable coercer or violator who has "caused" poverty or unemployment, and thus without a coercer, there can be no legitimate claim of justice. For Hayek, the market is a decentralized and impersonal process. Incomes and distributive shares "are the outcome of a process the effect of which on particular people was neither intended nor foreseen by anyone when the institutions first appeared," and "to demand justice form such a process is clearly absurd, and to single out some people in such a society as entitled to a particular share evidently unjust" (65). Since these claims of justice cannot identify a specific person who has been unjust, there is no one against whom to make a claim. As a result, the idea of justice "has no application to the manner in which the impersonal process of the market allocates command over goods and services to particular people: this can be neither just nor unjust, because the results are not intended or foreseen, and depend on a multitude of circumstances not known in their totality to anybody" (70). Hayek thus rejects claims of socioeconomic rights and efforts to establish a welfare state, because in a decentralized market system, it is unclear against whom these claims are make.

[12] See e.g., Lindblom, *The Market System*, 90-2, 171-2, 188.

possibility, constituting a deeper threat to the very idea of agency. Although any wealthy society can afford a range of different socioeconomic regimes, a real interrogation of alternatives is limited by a constrained discourse that is overly bound by the market as a way of thinking.[13]

The challenge, then, is to *repoliticize* the functioning of the market—to make it a subject of political debate, a system amenable to reformulation and human agency. This repoliticization can partly be achieved through private association. The trade union and consumer rights movements, for example, highlight how individuals can form associations to force accountability and changes in the behavior of private actors and market participants. In the financial crisis, NGOs and community groups played a large role in mobilizing to pressure banks to alter their lending policies. But the state must necessarily play a role, for the state offers a source of coercive power that can be deployed to oversee and regulate such exercises of private and market power at a macro level. Indeed, it is equally notable that the efforts of citizen and consumer watchdog groups were insufficient to prevent predatory lending prior to the 2008 crash—and the successes of such popular mobilization often depend on eventual policy responses from the state to generate broad impact. It is through the state that we achieve the collective capacities and power to reshape the economy as a whole.

Where there is a problem of private power, the need is to ensure democratic accountability of economic—and governmental—elites.[14] To respond to the problems of market society, the state emerges as a critical instrumentality through

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[13] Charles Lindblom, "The Market as Prison," *Journal of Politics* 44:2 (1982), 324-36, at 333-4.

[14] See e.g. Lindblom, *Market System*, 65-8.

which affected citizens can be sufficiently empowered in their ability to contest and check the exercises of private or market power. The problem of private power suggests a motivation for some forms of regulation like antitrust, workplace safety, and campaign finance. Where there is a problem of systemic or market power, the need is to develop policies that ensure basic minimum standards of welfare and well-being. The problem of market power points to the value of other major innovations in economic and social policy: minimum standards such as wage floors and consumer protections;[15] subsidies to enable basic needs to be accessible to all such as food stamps; and social insurance schemes that seek to insulate individuals from the dynamics of market supply and demand in key areas,[16] such as unemployment insurance and health insurance.

More broadly, such policies can be justified as providing, through politics, the collective goods that we all require to enjoy fulfilling life opportunities.[17] This grounding for economic regulation contrasts with market-based views of freedom as individual choice over commodities valued on the basis of their market price.[18] This agency-based view of regulation also contrasts with technocratic understandings of economic policy that view the substantive goals of regulation in more narrow terms of closing of market failures or optimizing market functioning. In mainstream contemporary discourse, regulation rarely refers to the ultimate

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[15] See e.g. Joseph Singer, "Things That We Would Like to Take for Granted: Minimum Standards for the Legal Framework of a Free and Democratic Society," *Harvard Law and Policy Review* 2 (2008), 139-160.

[16] See e.g. David Moss, *When All Else Fails: Government as the Ultimate Risk Manager* (Cambridge: Harvard University Press, 2002).

[17] See e.g. Elizabeth Anderson, "The Ethical Limitations of the Market," *Economics and Philosophy* 6 (1990), 179-205, at 192-5.

[18] Anderson, "Ethical Limits of the Market," 180-2.

moral ends of markets, preferring to focus on more neutral goals of efficiency and growth. The purposes of regulation can be understood more broadly as providing collectively-valued moral ends and goods—goals which necessarily require institutional coordination across individuals and groups to jointly produce these ends and goods.[19]

This emphasis on agency, however, also carries implications for the process by which such economic policies are developed. If private power and market power threaten individual agency, so to does the potential power of the state. Democratic accountability and voice offer the promise of checking such state power, by transforming the action of the state from an external imposition into an *expression* of our own collective agency. Agencies should not be seen as sites of rationality, but rather as sites of democratic action—spaces in which citizens can participate, engage, and thereby experience democratic self-government. Indeed, this view of agency requires that we create institutions that can facilitate the collective action of citizens, particularly on matters of economic justice, for it is through collective political action that these substantive goals can and must be met.[20] This poses a challenge for regulatory institutions, which operate at a remove from democratic politics.

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[19] See e.g. Seumas Miller, "Global Financial Institutions, Ethics, and Market Fundamentalism," in Ned Dobos, Christian Barry, and Thomas Pogge, *Global Financial Crisis: The Ethical Issues* (London: Palgrave MacMillan, 2011), 24-51, at 32, 38.

[20] See e.g. Anderson, "What is the Point of Equality?" 309-10, 313.

Technocracy as a threat to agency

Much of the substantive policies of the modern regulatory state can therefore be justified as addressing the moral problems of private and market power. But this agency-based view also carries important implications for the ways in which such regulation is structured and exercised. The instrumentalities of the state, even if directed to these justified goals of contesting private and market power, pose their own threat to agency to the extent that state regulatory institutions fall prey to interest group capture, unaccountability, and unresponsiveness. The financial crisis, for example, suggests the need for greater oversight by regulatory agencies like the SEC, while also underscoring the degree to which these agencies, insulated from ordinary channels of democratic accountability, are themselves at risk for being captured by industry, or being inadequately responsive to the public. If private and market power undermine the claims of free market defenders, so too does this concern with public power undermine the appeal to technocracy as a response to the problems of the market.

In the same way that the concept of agency highlights the problems of the market economy, it also lends credence to laissez-faire critiques of the state. As suggested in Chapter 3, laissez-faire thought drew on an institutional sociology describing the market as more robust to corruption, more efficient in its use of information, more adaptable and responsive to the diversity and complexity of modern society. The market, in this view, is an effective social institution can organize and coordinate social activity not through central planning, but through the aggregated interactions between individual market participants; as a result the market can achieve socially beneficial collective outcomes such as product innovation, growth, and the allocation of goods and services without relying on

the superhuman knowledge or virtue of individual rulers or decision-makers.[21] The normative vision of freedom as negative liberty is thus paired with an institutional sociology that presents the market as a more reliable, effective, and relatively corruption-proof mechanism for realizing these normative ideals and promoting overall social welfare and justice.[22] This is what makes the laissez-faire critique so compelling an attack on technocratic institutions: it is not just a rejection of the state, but a combined moral and institutional critique of the state—and a constructive defense of the market as an alternative. To the extent that modern societies have failed to promote justice or growth, it is because our institutions for public policy lack the robustness to corruption, the efficiency, and the responsiveness to individual preferences and changing conditions exhibited by the market system itself; we would instead, in this argument, be better served by promoting decentralized preference-aggregating institutions like markets to better promote welfare, justice, and liberty.[23]

As suggested in Chapter 4, the modern technocratic vision tries to absorb these concerns by doubling down on the expertise, neutrality, and objectivity of regulators themselves. It also attempts to restore the legitimacy of technocratic regulation by adopting market-based regulatory strategies, such as the use of cost-benefit analysis, public-private partnerships, and minimalist light-touch regulatory

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[21] See e.g. Hayek, "The Use of Knowledge in Society," in *Essence of Hayek*, 211–24; Lindblom, *The Market System*, 4-50.

[22] See e.g. John Tomasi, *Free Market Fairness* (Princeton: Princeton University Press, 2012).

[23] See e.g. Margaret Somers, Fred Block, "From Poverty to Perversity: Ideas, Markets, and Institutions over 200 Years of Welfare Debate," *American Sociological Review* 70:2 (2005), 260-287 (arguing that the rise of market fundamentalism in welfare reform debates in the 1980s and 1990s arose in part from the epistemic clout of free-market thinking that explained the persistence of poverty and the failures of public policy as a result of both a moral and an institutional-sociological failure.)

strategies like disclosure aimed at optimizing rather than constraining market functioning.[24] But these efforts cannot overcome the laissez-faire challenge because the technocratic ideal ultimately undermines the same value of agency that motivates the turn to the state in economic governance in the first place. In other words, while the policies problems of private and market power pose threats to individual and collective agency—thus motivating the turn to state regulatory regimes—the technocratic regulatory state itself institutionalizes these policies in ways that risk undermining agency from a different direction.

First, the appeal to insulated, technocratic institutions of governance is insufficient to overcome the danger of potential domination of citizens by private actors and social elites. While the model of insulated technocratic decision-making is often motivated as a response to the dangers of special interests capturing institutions of the state to pursue their own private agenda, the narrowing of space for participation can just as easily facilitate the situation of various forms of elite domination. Without the check provided by robust participatory institutions, it seems likely that economic and political elites will arrogate unto themselves excess state and private power.[25] Indeed, well-connected and sophisticated political actors—such as regulated industries, corporations, and social elites more

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[24] See e.g. Chapter 4 above.

[25] See John McCormick, "Machiavelli Against Republicanism: On the Cambridge School's Guicciardinian Moments," *Political Theory* 31:5 (2003), 615-643; "Contain the Wealthy and Patrol the Magistrates: Restoring Elite Accountability to Popular Government," *American Political Science Review* 100:2 (2006), 147-163; and *Machiavellian Democracy* (New York: Cambridge University Press, 2011). McCormick argues that the elites who threaten contemporary democracies are in fact the wealthy, and that greater participatory institutions are needed to strengthen the political power of ordinary citizens as a check on elite interests. See also Ian Shapiro, *The State of Democratic Theory* (Princeton: Princeton University Press, 2003). Shapiro argues that "democracy is better thought of as a means of managing power relations so as to minimize domination," (3) but that in so doing, democracy must therefore expand the range of political contestation and pay particular attention to problems of economic domination and inequality.

generally—are more likely to continue to be able to influence policy making despite the range of barriers erected to protect technocratic bodies, while it is precisely those less organized, less sophisticated actors who are likely to be screened out by such insulation. The effort to construct insulated regulatory bodies thus risks creating and compounding problems of misrepresentation and inequalities of political power.

Second, the efficiency and effectiveness gains of technocratic policy making often presume that the public good is a determinate object to be executed, having already been identified or established through some legislative or other political mechanism. Yet it is precisely in the effort to articulate and construct a common good in a complex society that democratic politics emerges as vital. The participation of the public and the groups beyond technocrats and elites, it is unclear what exactly the common good might be. It is only for inclusive political discussion and participation that provisional understandings of the common good can be articulated in the first place. Nor is it sufficient to rely solely on the national legislature, since the same normative value considerations and balancing of interests reappears at various stages of regulatory policymaking. Both the threat of elite influence and the need for inclusive participation to construct the public good suggest the technocratic regulatory state, with its focus on insulated expert policymakers, undermines political agency even as it attempts to resolve problems posed by market society.

There is a deeper problem, however: the very structure of depoliticizing technocratic governance threatens the broader vitality of democratic agency itself. While the technocratic impulse may promote the common good by insulating certain policy decisions from the influence of the democratic majority or other

special interest groups, as this impulse becomes more widespread, the very concept of democratic self-governance becomes displaced. These technocratic institutions "usurp" the democratic agency of citizens—even if their policies were to effectively track the common good. As Patchen Markell writes, depoliticization

> might be at the same time useful for and dangerous to democratic politics: the very mechanisms by which we effectively avoid certain forms of domination (like majoritarian tyranny) may simultaneously have the effect of undermining citizen involvement in the everyday practice of governance by presenting certain matters as the special province of experts or professionals, or by removing the conduct of depoliticized institutions from public view.[26]

Citizen participation contestation is critical to check the arbitrary power of the state, as well as the power of other interests, but citizens will only participate if they see such engagement as intrinsically valuable.[27] The danger of the technocratic framework is that not only does it narrow the scope for democratic agency, it gradually contaminates and hollows out the very concept. The proliferation of depoliticized bodies devalues political participation at best, openly feeds a rejection of the value of democratic participation at worst. The result can be a dangerous undermining of the participatory ideal, to the point where citizens themselves become increasingly demobilized and disconnected from politics. The effort to curtail participation because of a fear of majority tyranny by placing greater power in insulated technocratic bodies is therefore problematic because of its broader demobilizing effects.

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[26] Patchen Markell, "The Insufficiency of Non-Domination," *Political Theory* 36:1 (2008), 9-36, at 29.

[27] Markell, "Insufficiency of Non-Domination," 29.

In search of a more democratic regulatory state

The problems of the market and of technocracy suggest that the value of agency takes on multiple dimensions. Not only are there threats to agency from private and market power as identified by Progressive critics of the market; there are also threats from unaccountable state institutions as highlighted by laissez-faire thinkers. Taken together, these critiques point to the value of a more democratic approach to economic regulation. It suggests that we view regulation not as the province of insulated, neutral experts managing the market economy in the name of the public good, but rather that we approach regulation as a distinctly *democratic* project, where citizens collectively engage in the practice and experience of self-government, through direct participation in the crafting of those regulations and rules that shape the workings of the economy itself.

In this "agency conception" of the regulatory state, regulation becomes more than a residual response to the market, or even a system for redistribution and provision of basic needs mechanism; instead it is more importantly a *political* apparatus for facilitating cooperation and political action on economic matters.[28] The purpose of the regulatory state, in this broader view, is to enable the ongoing political capacity of individuals to reshape economic society—the state provides both the forum in which these debates can take place, and the instrumentalities through which responses are made real. In turn, these state institutions must themselves be contestable by individuals so as not to create another threat of unaccountable public power.

[28] See e.g. Joseph Heath, "The Benefits of Cooperation," *Philosophy and Public Affairs* 34:4 (2006).

Further, by putting the normative value of agency at the center, this account of economic regulation also suggests that regulatory agencies themselves must be constituted in a particular way. It is not enough, for example, to implement a redistributive program through a highly centralized and insulated bureaucratic apparatus, since the goal is not purely a shift in income or risk. Rather, these policies must themselves be enacted in ways that continue to facilitate and expand the agency capacity of individuals—their ability to be political actors empowered to continually remake their economy and society as needed. This suggests that regulatory agencies cannot simply implement policy directives; rather they must do so in ways that supplement rather than supplant the political agency of citizens themselves. For example, economic regulation may well require the use of experts, and an insulation from certain kinds of electoral politics. But this turn to expertise and insulation can be dangerous if it results in a supplanting of the political agency of ordinary citizens, by further narrowing the scope for and contexts of political action.[29] The challenge then becomes a matter of navigating this tension between harnessing the institutions of the state to respond to the problems of the market, while also ensuring that such state action remains accountable and responsive to the citizenry itself.

This agency-based argument thus distills and clarifies the fundamental challenge for economic governance today. On the one hand, the problems of the market economy—private and market power—demand the creation of state institutions and policies that can address these threats to individual and collective agency. These institutions would not only check exercises of private and market

[29] See e.g. Markell, "Insufficiency of Non-Domination".

power; they would do so in a way that magnifies the agency of citizens to govern their own economic futures. But the very institutions we create to meet this need themselves pose a threat to agency. To the extent that the complexity of addressing private and market power induces us to build regulatory agencies that emphasize expertise over the seemingly dangerous instabilities of democratic politics, these institutions by their very separation from democracy raise their own potential threats to agency. As Gerald Frug writes,

> Bureaucracy is the primary form of organized power in America today, and it is therefore a primary target for those who seek liberation from modern forms of human domination. The ideology that reassures us that bureaucracy is legitimate is demobilizing because it conceals the need to reorder American society to bring to life better versions of the ideal of human freedom.[30]

The only alternative, for Frug, is to build an alternative institutional structure that ensures such an ideal of freedom where citizens can "creat[e] for themselves the form of organized existence within which they live."[31]

Viewed from the standpoint of agency, then, both free markets and technocracy do not simply rationalize economic governance; they sterilize it, and remove it from the scope of our collective agency. This makes their failures particularly difficult to undo, overcome, or revise. Like the market, the appeal of technocracy is precisely that regulators themselves are insulated from the corruption, irrationality, and political distortions of ordinary democratic politics. By removing policy decisions from the reach of democratic politics, technocracy attempts to at once depoliticize these issues, to immunize them from democratic

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[30] Gerald Frug, "The Ideology of Bureaucracy in American Law," *Harvard Law Review* 97 (1983-4), 1276-1388, at 1294.

[31] Frug, "Ideology of Bureaucracy," 1296.

contest, and in so doing achieve the necessary latitude to make socially-optimal policy decisions. Such depoliticization emaciates the very value of agency at both the level of individuals and societies.[32]

This commonality points to the reasons why technocracy cannot generate the kind of response needed to the laissez-faire critique. In its distrust of politics, and in its effort to absorb the criticisms of laissez-faire, it divorces itself from the moral energies that could animate and sustain the reform aspirations with respect to the market—a substantive vision of economic justice, or an appeal to the democratic agency of citizens. But what then is the alternative? To the extent that technocratic institutions suffer from potential problems of capture, corruption, or unresponsiveness, the laissez-faire solution of deregulation is untenable because that simply trades one threat to agency for another, the threats of the market for the threats of the regulator. The answer, I suggest, is to reconstitute the state's role in economic governance as a more deeply democratic project. The problem of economic governance thus suggests the need for *both* a more robust regulatory role for the state, *and* institutions and practices to subject such regulatory actions to democratic contestation, sanction, and ownership. Where the instrumentalities of the state are too removed from such democratic contest, then the state's actions however well-intentioned as a response to private and market forms of domination itself raises the specter of unaccountable and potentially arbitrary power.

This concern about the tension between democratic self-rule and the exercise of regulatory authority has been a central concern in debates over the regulatory state since the New Deal. Contemporary administrative law purports to

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[32] See e.g. Patchen Markell, "Rule of the People: Arendt, Arche, and Democracy," *American Political Science Review* 100:1 (2006), 1-14.

have resolved this tension through institutional arrangements that bind regulatory agencies to serving the public good as determined by legitimate democratic procedures. But as we shall see in the next chapter, these attempts are flawed, in effect sanctifying and reproducing the basic problem of technocratic authority that is exercised too far removed from the contestation and voice of democratic citizens. We therefore need a better theory of democracy that rescues and reconstitutes the regulatory state as a vehicle for addressing the problems of private and market power. As the next chapter suggests, administrative law claims but fails to provide such an account—but it does provide some resources for the development of such a theory.

6 THE PROMISE AND LIMITS OF ADMINISTRATIVE LAW

The challenge for the modern regulatory state is to find a way to harness its capacities for responding to the threats of private and market power, but to structure its authority such that it is an expression of the democratic citizenry. The moral value of regulation derives from the degree to which the practice of regulation manifests the collective capacities of the citizenry to self-govern—to remake the social and economic order through politics. The more regulation is seen as an external imposition, an exercise of authority unaccountable and unresponsive to the citizenry, this moral foundation erodes. This is the very concern raised both by critics of technocracy and laissez-faire attacks on the state.

Contemporary administrative law purports to reconcile the exercise of regulatory authority with the ideals of democratic self-government through one of two main theories: binding agencies to the democratically-sanctioned public good through robust oversight of regulation by elected officials; or by recasting agencies as sites of expert-led deliberation over the common good in which citizens may be consulted. But these accounts ultimately fail. Even as they proclaim on the surface the moral importance of constituting regulation as an expression of democratic self-government, the dominant theories of regulation in administrative law create too large a gap between the role of citizens on the one hand, and the actual exercise of regulatory authority on the other. To the extent that administrative law offers resources for reconciling democratic self-rule with regulation, it is by

pointing to the value of institutionalizing greater forms of representation and participation within regulatory agencies.

Oversight, Non-domination, and their limits

Starting in the late 1990s, Jeffrey Skilling, the leader of Enron, led his company to an unprecedented run of record returns. Skilling's use of new financial leverage and accounting techniques earned him a reputation as a genius. Yet by 2006 Skilling was in jail, his company and his accounting firms collapsed. Skilling's success had been built on an accounting illusion that, once revealed, led to the Sarbanes-Oxley Act of 2002. In retrospect, the Enron scandal was a dress rehearsal for Dodd-Frank. The techniques used by Skilling would later be perfected by Lehman Brothers and other Wall Street firms, who used similar "special investment vehicles" and "special purpose entities" to engage in massively leveraged risky bets without appearing on official balance sheets.[1] The response to the accounting scandal, like Dodd-Frank eight years later, sought to prevent future disasters by creating a new regulatory agency to oversee the accounting industry: the Public Company Accounting Oversight Board (PCOAB). To ensure the Board's protection from special interests, it was constituted as a highly expert body, whose members would be chosen by, but would serve independently of, the SEC commissioners—who themselves were chosen by but independent of the president.

[1] See e.g., William Bratton, Adam Levitin, "A Transactional Genealogy of Scandal: From Michael Milken to Enron to Goldman Sachs," University of Pennsylvania Law School, Institute for Law and Economics, Research Paper No. 12-26; Georgetown University Law Center, Public Law and Legal Theory Working Paper Series No. 2126778 (August 13, 2012).

In 2010, the Supreme Court struck down this "dual for-cause" structure in the case of *Free Enterprise Fund v. PCOAB*.[2] The case is notable because the argument between majority and dissent in the case highlights the two main rival theories of the regulatory state in contemporary administrative law: the majority's theory of regulation under robust oversight by elected officials, and the dissent's theory of regulation guided by insulated expertise as a legislatively-sanctioned process. Both of these theories justify broad regulatory authority as consistent with, and an expression of, the ideal of democratic self-government. Yet the debate between the two sides underscores the degree to which both of these accounts are misleading, for in practice, neither does much to address the criticisms of technocratic governance as too far removed from the political agency of citizens themselves.

In his majority opinion, Chief Justice John Roberts argued that to be consistent with democratic self-rule, agencies had to be directly accountable to and overseen by the democratically-elected president. The dual for-cause structure was therefore unconstitutional, for it created too large a gap between the PCOAB's activities on the one hand, and their accountability to the public through the figure of the President on the other. As a result,

> neither the President, nor anyone directly responsible to him, nor even an officer whose conduct he may review only for good cause, has full control over the Board. The president is stripped of the power our precedents have preserved, and his ability to execute the laws—by holding his subordinates accountable for their conduct—is impaired.[3]

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[2] *Free Enterprise Fund v. Public Company Accounting Oversight Board*, 130 S. Ct. 3138 (2010).

[3] *Free Enterprise Fund,* 130 S. Ct., at 3154.

The problem with such a "diffusion of power" is that it "carries with it a diffusion of accountability," muddling the "clear and effective chain of command," and ultimately undermining public's ability to hold agencies and president to account.[4]

In dissent, Justice Stephen Breyer leads the liberal bloc on the Court defending the insulation of the PCOAB as a necessary protection for regulatory expertise. The majority opinion, writes Breyer, "threatens to disrupt severely the fair and efficient administration of the laws," which in turn undermines the ability of the state to promote the public good.[5] In order to achieve efficient and effective governance, Congress must have the flexibility to develop alternative institutional forms for agencies. In some cases, good public policy will require heavy insulation from politics—just as Ulysses tied himself to the mast, so too must the political branches divest themselves of direct oversight of certain policy areas.[6] Such delegation is sanctioned by—and thus represents an expression of—the democratic public will. The majority opinion, for Breyer, creates the terrifying prospect of undermining much of the vast apparatus of the modern regulatory state:

> Reading the [majority's] criteria above as stringently as possible, I still see no way to avoid sweeping hundreds, perhaps thousands of high level government officials within the scope of the Court's holding, putting their job security and their administrative actions and decisions constitutionally at risk.[7]

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[4] *Free Enterprise Fund,* 130 S. Ct., at 3155.

[5] *Free Enterprise Fund,* 130 S. Ct., at 3162.

[6] *Free Enterprise Fund,* 130 S. Ct., at 3168-69.

[7] *Free Enterprise Fund,* 130 S. Ct., at 3180.

To the extent that unaccountable agencies are a problem, the technocratic nature of the agencies should be sufficient, in Breyer's view, to assuage any concerns of unaccountable agency power. The PCOAB members are "technical professional experts," working in an apolitical independent agency, who must be "insulate[d]" from "political influences".[8]

Both Roberts and Breyer couch their theories of regulation in a similar appeal to the fundamental ideal of democratic self-rule. In his other writings, Breyer espouses a commitment to the "freedom of the individual citizen to participate in the government and thereby to share with others the right to make or to control the nation's public acts."[9] Expert deference is consistent with such "active liberty" as a way of respecting the implicit will of the democratic legislature in empowering such experts in the first place—and as a way of ensuring that public policy promotes the common good, as understood by these experts.[10] Roberts counters Breyer's appeal to politically-insulated and neutral expertise by emphasizing the moral value of self-government:

> One can have a government that functions without being ruled by functionaries, and a government that benefits from expertise without being ruled by experts. Our Constitution was adopted to enable the people to govern themselves, through their elected leaders. The growth of the Executive Branch, which now wields vast power and touches almost every aspect of daily life, heightens the concern that it may slip from the Executive's control, and thus from that of the people. This concern is largely absent from the dissent's paean to the administrative state.[11]

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[8] *Free Enterprise Fund,* 130 S. Ct., at 3174.

[9] Stephen Breyer, *Active Liberty: Interpreting Our Democratic Constitution* (New York: Vintage Books, 2005), 3.

[10] Breyer, *Active Liberty*, 103-6.

[11] *Free Enterprise Fund,* 130 S. Ct., at 3156.

But this assumption of the mantle of democratic self-government is belied in both theories by the tremendous gulf they create between the role of citizen action on the one hand, and the exercise of regulatory authority on the other. Roberts and Breyer each instantiate two rival normative traditions of democratic self-rule applied to the modern regulatory state. Roberts' oversight view builds on a traditional view of democratic self-rule as secured by the republican separation of powers. Breyer's defense of expertise, by contrast, rests on an underlying theory of non-domination which provides a different reconciliation between democratic self-rule and regulatory expertise. But both of these theories, for all their democratic veneer, ultimately place the citizen far removed from the actual exercise of regulatory authority. For the oversight and separation of powers view, citizens engage in political contestation, but far upstream from regulatory policymaking. For the non-domination view, citizens have a greater role within regulatory agencies, but only as apolitical deliberators, without the full range of political powers to actually contest regulatory policies.

The limits of oversight

In traditional Constitutional theory, the exercise of state authority is rendered legitimate and consistent with the public good when it is subjected to adequate political contestation, secured through the constitutional scheme of the separation of powers. By dispersing state power and ensuring checks and balances

between the branches of executive, legislature, and judiciary, tyrannical state action could be prevented and liberty guaranteed.[12]

The separation of powers served as the first normative and institutional framework that critics of the emerging regulatory state harnessed to reconcile regulatory authority with political freedom. These early critics saw agencies as a threat to liberty precisely because they defied this constitutional separation of legislative, executive, and adjudicatory functions: agencies, although formally part of the executive branch, threatened to exercise legislative or adjudicatory functions. Thus, the Court strove to prevent agencies from exercising judicial functions as a violation of the Constitutional grant of judicial authority to the courts, or from being empowered by overly broad delegations of legislative authority as a violation of the Constitutional grant of legislative authority to Congress. These measures sought to limit agency authority, preserve the separation of powers, and therefore ensure liberty.[13] But because legislative, executive, and judicial functions could not be so easily disentangled,[14] and because of the persistent concern about the need to ensure "effective functioning of a

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[12] Rebecca Brown, "Separated Powers and Ordered Liberty" *University of Pennsylvania Law Review* 139 (1990-1), 1513-1566, at 1513-16. See also James Madison, *Federalist Papers*, Nos. 47, 48, 51 in Ian Shapiro, ed., *The Federalist Papers* (New Haven: Yale University Press, 2009).

[13] See e.g., *Humphrey's Executor v. United States,* 295 U.S. 602 (1935) (upholding Congressional interference with Presidential removal powers); *A.L.A. Schechter Poultry Corp. v. United States*, 295 U.S. 495 (1935) (invalidating the National Industrial Recovery Act as an impermissible delegation of legislative powers).

[14] *Bowsher v Synar*, 478 U.S. 714 (1986). See especially 478 U.S. at 751: "One reason that the exercise of legislative, executive, and judicial powers cannot be categorically distributed among three mutually exclusive branches of government is that governmental power cannot always be readily characterized with only one of those three labels. On the contrary, as our cases demonstrate, a particular function, like a chameleon, will often take on the aspect of the office to which it is assigned."

complex modern government,"[15] the Court shifted to a more permissive stance.[16] Thus, although the Court occasionally ruled against agencies for mixing the different constitutional functions,[17] by and large agencies would be left alone.[18]

Today, this separation of powers framework reappears in a different guise through the oversight approach. This theory appears not only in the administrative law decisions of Justices John Roberts and Antonin Scalia; it is also prominently associated with Justice Elena Kagan's prior work as a legal scholar.[19]

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[15] *INS v. Chadha*, 462 U.S. 919 (1983), J. White dissenting, 462 U.S. at 989 ("If the effective functioning of a complex modern government requires the delegation of vast authority which, by virtue of its breadth, is legislative or 'quasi-legislative' in character, I cannot accept that Article I—which is, after all, the source of the non-delegation doctrine—should forbid Congress from qualifying the that grant with a legislative veto.")

[16] See e.g. Peter Strauss, "Formal and Functional Approaches to Separation-of-Powers Questions—A Foolish Inconsistency?" *Cornell Law Review* 72 (1986-7), 488-526. *Myers v. United States*, 272 U.S. 52 (1926), J. Brandies, dissenting at 85 (noting friction between the constitutional branches is designed to prevent autocracy).

[17] See e.g., *Chadha*, 462 U.S., at 944 (rejecting claim to administrative efficiency in defense of constitutional liberty).

[18] For the weakening of Article I restraints on delegations of legislative authority to agencies, compare for example, *Schechter*, 295 U.S. with *Whitman v. American Trucking Associations, Inc.*, 531 U.S. 457 (2001) (delegations of legislative authority to agencies is permissible so long as these delegations come with an "intelligible principle" that guides the agency's exercise of the delegated authority), and *Chevron USA Inc. v. Natural Resources Defense Council*, 467 U.S. 837 (1984) (Judicial deference to agency interpretations of law justified as deference to inferred Congressional intent to delegate discretionary authority to the implementing agency). For the weakening of Article III restraints on agencies exercising judicial powers, see for example, *Bowsher* and related cases. The same "flexible understanding of the separation of powers" animating *Bowsher v. Synar* led the Court to uphold a delegation of rulemaking power to the Sentencing Commission placed under the judicial branch, since this delegation did not "trench upon the prerogatives of another Branch" and was "appropriate to the central mission of the Judiciary." *Mistretta v. United States*, 488 U.S. 361 (1989), at 381 and 388. Similarly, after early attempts to limit their reach to "public" rather than "private" rights,[18] *Crowell v. Benson*, 285 U.S. 22 (1932); *Northern Pipeline v. Marathon Pipe Line Co.*, 458 U.S. 50 (1982), now departures from Article III courts are permissible in light of the policy considerations that may drive Congress to allocate certain adjudicatory functions to expert agencies. See *Commodity Futures Trading Commission v. Schor,* 478 U.S. 833 (1986), and *Northern Pipeline*, 485 US, White dissenting. See also *Atlas Roofing v. Occupational Safety and Health Review Commission*, 430 U.S. 442 (1977) (Upholding adjudicatory actions by OSHA against a Seventh Amendment challenge on grounds of administrative efficiency and institutional competence).

[19] See e.g. Elena Kagan, "Presidential Administration," *Harvard Law Review* 114 (2001), 2245-2385.

In the oversight theory of democratic regulation, once policies are forged through the political process involving electoral contestation around the selection of representatives plus political contestation through inter-branch checks and balances between legislative, executive, and judicial functions, they bear the stamp of the public will, and can then be straightforwardly implemented by regulatory institutions that are positioned 'downstream' from the domain of political contestation. In this view, the problem of regulatory authority is defused and reconciled with democratic ideals by ensuring the smooth functioning of core democratic processes of contested elections and checks and balances between executive, legislative, and judicial branches. These modes of contestation would ensure that the exercise of regulatory authority, so long as it is subject to oversight by politically and constitutionally accountable branches of government, remains consistent with democratic agency.

But the problem with this oversight approach is that such political contestation through elections and inter-branch checks and balances is ultimately too attenuated from the political and moral judgments that inextricably are part of regulatory policymaking. As Richard Stewart rightly noted long ago, such "transmission belt" understandings of regulation as merely "implementing legislative directives in particular cases" are far-fetched.[20] Regulatory agencies routinely have to make both technical and normatively-inflected policy judgments within a relatively wide range of discretion and authority accorded under Congressional sanction and presidential oversight—they do not simply execute specific Congressional commands.

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[20] Richard B. Stewart, "The Reformation of American Administrative Law," *Harvard Law Review* 88:8 (1975), 1669-1813, at 1675.

Furthermore, neither Congress nor the executive directly oversees or controls every regulatory rule or judgment; the scope of the regulatory state is too vast. Although the theory of presidential administration holds that agencies are checked by the ability of a democratically-elected executive to coordinate and guide policymaking, top-down direction of agencies may not be enough to fully respond to concerns of agency accountability and legitimacy. Presidential oversight appears as more of a placeholder, "a sign of how desperately we needed a way to legitimate the regulatory enterprise and to answer growing criticism of the procedural and substantive rationality of regulation."[21] Meanwhile, regulatory agencies are legally empowered to offer their own interpretations of ambiguous Congressional statutes.[22] The Supreme Court has justified such agency deference as couched in respect for implicit Congressional sanction. But this simply papers over a persisting anxiety that regulatory agencies exercise legislative authority beyond the scope and oversight of Congress.[23] Indeed, there is continuing unease in legal doctrine over when and how much courts should defer to agency interpretations of

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[21] Cynthia Farina, "Undoing the New Deal Through the New Presidentialism," *Harvard Journal of Law and Public Policy* 22 (1999), 227-238, at 232. See also Cynthia Farina, "Statutory Interpretation and the Balance of Power in the Administrative State," *Columbia Law Review* 89 (1989), 452-528, at 515 (noting that the presidency is not a substitute for democratic legislative control as it reflects a different political base and presidential policy does not develop through procedures requiring representative debate and acceptance).

[22] See *Whitman,* 531 U.S. (2001) (delegations of legislative authority to agencies is permissible so long as these delegations come with an "intelligible principle" that guides the agency's exercise of the delegated authority), and *Chevron*, 467 US (1984) (Judicial deference to agency interpretations of law justified as deference to inferred Congressional intent to delegate discretionary authority to the implementing agency).

[23] See Farina, "Statutory Interpretation, at 456 ("By portraying the choice of deference as an affirmation of legislative primacy and an enhancement of democratic control over the regulatory process, *Chevron* appeals to our deepest constitutional unease about allocating power in the administrative state. Ultimately, however, we cannot embrace *Chevron's* vision of deference as the handmaiden to separation of powers and legitimacy principles without substantially recasting those principles-a recasting in which some aspects of existing theory would have to be abandoned and others radically reformulated").

Congressional statutes.[24] Finally, voters themselves have an even more attenuated connection to the final rules and judgments issued by agencies.

Non-domination and its limits

In contrast to the oversight theory, Breyer's defense of regulatory expertise is part of a broader normative account of democracy and regulation shared with a range of other thinkers like Philip Pettit and legal scholars like Cass Sunstein. These "non-domination" theories provide a stronger normative foundation for expansive state regulation. In these accounts, the problem of domination—nonarbitrary interference with individual actions—can take place not only through unaccountable state actors but also through unaccountable private actors such as corporations or market actors. The state is therefore justified in regulating such exercises of power in the name of protecting, rather than undermining, individual freedom. In these accounts, the ideal of non-domination can motivate and justify forms of state intervention that, while responding to social challenges such as domination and economic hardship, may otherwise trouble defenders of the more narrow liberal or libertarian view of the state.[25]

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[24] See e.g. *United States v. Mead Corporation*, 533 U.S. 218 (2001) (attempting to limit when Chevron applies); *Gonzales v. Oregon*, 546 U.S. 243 (2006) (denying deference for regulations that simply restate statutory language, in an effort to prevent agency self-dealing); *Food and Drug Administration v. Brown & Williamson Tobacco Corporation*, 529 U.S. 120 (2000) and *MCI Telecommunications Corp. v. American Telephone & Telegraph Co*., 512 U.S. 218 (1994) (articulating a "nondelegation canon" for narrowly interpreting statutory grants of agency authority). See also, Farina, "Statutory Interpretation and the Balance of Power in the Administrative State," 456; Farina, "Deconstructing Nondelegation," *Harvard Journal of Law and Public Policy* 33 (2010), 87-102, at 95.

[25] See e.g. Philip Pettit, *Republicanism: A Theory of Freedom and Government* (New York: Oxford University Press, 1999), 148-62; Henry Richardson, *Democratic Autonomy: Public Reasoning About the Ends of Policy* (New York: Oxford University Press 2002), 28.

These non-domination theories thus possess a number of compelling features. First, they recapitulate much of the Progressive critique of laissez-faire, by highlighting the dangers of private power as well as public power. This in turn provides a substantive justification for why the powers of the state should be deployed to make economic policies and regulations. Second, they suggest that these policies must themselves be formulated in a manner consistent with democratic principles, in order to prevent the state from itself posing a risk of domination to citizens. This seems to speak to the anxieties surrounding the insulated, unaccountable expert regulator. This ideal of citizen deliberation and contestation of policymakers can ensure that such state power is not itself arbitrary or dominating, as it is bound to follow the results of deliberative procedures that ensure state action promotes the common good.[26]

Third, non-domination theories also suggest the democratic value and potential of regulatory agencies themselves. Following the non-domination approach, regulatory agencies should seek policies promoting the common good, arriving at these policies through deliberation. Rather than a raw conflict between interest groups seeking political power, such institutional structure could instead facilitate good faith deliberation over the common good, yielding more effective and normatively desirable public policies.[27] Agencies thus become more than simply the transmission of electoral or legislative democratic consensus, nor are they repositories of pure elite or expert authority; rather they are important *sites* of democratic politics, providing "an integral part of our distributed democratic

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[26] Pettit, *Republicanism*, 107; Richardson, *Democratic Autonomy*, 50-1.

[27] See e.g. Richardson, *Democratic Autonomy*; Cass Sunstein, "Interest Groups in American Public Law," *Stanford Law Review* 38 (1985), 29-87, at 30-32.

reasoning about what we ought to do" through their structure facilitating good faith deliberation.[28] These qualities make agencies potentially superior to legislatures since they can "nurture public deliberation and the discovery of shared public values."[29] As professionals and experts, regulators could facilitate a good-faith deliberative dialogue between stakeholders without prejudice.[30] By contrast, Congress had too often failed to make difficult political choices, blocked by conflicting interest group pressures, and hobbled by an unwieldy and inefficient legislative process.[31]

In this "deliberative conception of administration," the regulator emerges not as a mere bureaucrat or expert, but rather as the central figure in driving democratic dialogue.[32] As Cass Sunstein, himself a legal scholar and later administrator within the regulatory state, argued,

> the role of the administrator is not merely to reflect constituent pressures or to aggregate private interests. Instead, the purpose of the regulatory process is to select and implement the values that underlie the governing statute and that, in the absence of statutory guidance, must be found through a process of deliberation. …In deciding how to implement the statute, however, the administrator must deliberate about the relevant interests and not respond mechanically to constituent pressures.[33]

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[28] Richardson, *Democratic Autonomy*, 250.

[29] Robert Reich, "Public Administration and Public Deliberation: An Interpretive Essay," *Yale Law Journal* 94 (1984-5), 1617-1641, at 1617.

[30] See e.g. Jerry Mashaw, *Bureaucratic Justice: Managing Social Security Disability Claims* (New Haven: Yale University Press, 1983).

[31] See Mark Seidenfeld, "A Civic Republican Justification for the Bureaucratic State," *Harvard Law Review* 105 (1991-2), 1511-1576, especially 1518-22.

[32] Cass Sunstein, "Factions, Self-Interest, and the APA: Four Lessons Since 1946," *Virginia Law Review* 72 (1986), 271-296, at 282.

[33] Sunstein, "Factions," 282.

Administrative deliberation seems to offer a way to engage the range of affected interests without collapsing into the dangers of deadlock or capture that accompany interest group politics.[34] To the extent that agency policymaking involves normative and value considerations, it is the agency administrator that emerges as the preferred deliberator, who can neutrally and rationally engage and weigh all the relevant interests before choosing a course of action.[35] Such a model of administration seems to fulfill the aspirations of non-domination views of democracy and regulation.[36]

This account thus offers an even more robust normative defense of regulation as an expression of democratic freedom—both in its substantive policies in combating domination, and in its process of engaging stakeholders in rational, expert-facilitated deliberation. But in practice, this ideal of deliberation within regulatory agencies does little to check or channel the decisions of regulators themselves. Indeed, Pettit explicitly steers away from the idea of popular political participation as a mechanism for checking the arbitrary power of the state and other social actors, arguing that "such a participatory ideal is not feasible in the modern world, and in any case the prospect of being subject to the will of all is scarcely attractive."[37] Pettit's account reserves to these expert bodies, and *not* to the democratic public, the ability to author and initiate public policies.[38] Pettit

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[34] See e.g. Martin Shapiro, *Who Guards the Guardians? Judicial Control of Administration* (Athens: University of Georgia Press, 1988), 14-15.

[35] Sunstein, "Factions," 282; Shapiro, *Who Guards the Guardians?* 33.

[36] Seidenfeld, "A Civic Republican Justification for the Bureaucratic State."

[37] Pettit, *Republicanism*, 81.

[38] Pettit, "Republican Freedom and Contestatory Democratization," in Ian Shapiro and Casiano Hacker-Cordon, eds., *Democracy's Value* (New York: Cambridge University Press, 1999), 163-

argues in favor of a range of institutions and depoliticized technocratic bodies as the optimal means of preventing majority tyranny, and tracking common interests.[39]

Democratic participation in this account is therefore reduced to being the product of a virtuous elite class of policymakers who engage in public dialogue not because of a fundamentally equitable distribution of political power but out of his own civic-mindedness. In language evocative of the most glowing defenses of the wisdom and rationality of the technocratic state found in early defenders like James Landis, non-domination theorists like Pettit and Sunstein celebrate the regulatory state for its role in making public policy rational. Democracy becomes more of an afterthought, orchestrated by virtuous administrators at their discretion to win greater social support or glean relevant information from citizens.

This appeal to expertise and regulator-led deliberation reproduces the very anxieties of technocracy raised by critics of the regulatory state. It leaves too much room for elite influence and capture; it does not engage a broad swath of citizens to ensure balanced contestation of regulatory policies; it undermines the value of participation by filtering it through the policy preferences of the regulator.[40] This approach also raises a moral concern that in this appeal to deliberation, we may undermine core democratic values by placing too much faith and authority in the

190; Pettit, "Deliberative Democracy and the Discursive Dilemma," *Philosophical Issues* 11 (2001), 268-297.

[39] Philip Pettit, "Depoliticizing Democracy," *Ratio Juris* 17:1 (2004), 52-65.

[40] See e.g., Martin Shapiro, "APA: Past, Present, Future," *Virginia Law Review* 72 (1986), 447-482, at 478.

powers of neutral expertise, to the detriment of the political empowerment of citizens themselves.

Participatory theories of regulation

Oversight and non-domination approaches to reconciling democracy with regulation are limited because they place the citizen either too far upstream from regulatory authority, or do not provide meaningful opportunities for participation within regulatory policymaking. These theories do, however, suggest two important insights for reconciling democratic agency and regulation. First, self-rule requires citizens be empowered to engage in political contestation as in the oversight and separation of powers approach to check and channel state authority. But second, citizens have to be incorporated into regulatory policymaking itself—as in the nondomination view. More recently, a variety of administrative law scholars have sought to develop this kind of a more participatory view of regulation that provides a more robust role for citizens within the regulatory process. These accounts by themselves remain limited, but they provide some resources for imagining a more democratic regulatory state.

The lost promise of interest representation

As noted in Chapter 4 above, during the 1960s and 1970s, concerns about regulatory capture motivated courts and legal scholars to advocate for greater

interest representation within the regulatory process.[41] Meanwhile, War on Poverty legislation under the Johnson administration included a variety of provisions to ensure "maximum feasible participation" of stakeholders within the regulatory process.[42] With this emphasis on interest representation, late-century administrative law took as its goal "the provision of a surrogate political process to ensure the fair representation of a wide range of affected interests in the process of administrative decision."[43] These efforts were abandoned, but they retain an unrealized potential as a mechanism for democratizing the regulatory state.

Consider for example the case of *Office of Communications of United Church of Christ v. FCC*.[44] In this case, the United Church attempted to intervene in an Federal Communications Commission (FCC) licensing decision for a local TV station in Mississippi arguing that the station was promoting a pro-segregation agenda. The FCC denied the church standing to participate in the proceeding, arguing that only full parties, applicants, or those suffering a "direct substantial injury" had the right to participate. The court, however, expanded the standing of stakeholder groups such as the church to participate in the licensing proceedings. Although the FCC itself represented the public interest, it could not, the court reasoned, effectively represent a full understanding of the public interest "without

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[41] See Stewart, "The Reformation of American Administrative Law"; Christopher Edley, Jr., *Administrative Law: Rethinking Judicial Control of Bureaucracy* (New Haven: Yale University Press, 1990), 215-222.

[42] See Noel Cazenave, *Impossible Democracy: The Unlikely Success of the War on Poverty Community Action Programs* (Albany: State University of New York Press, 2007).

[43] Stewart, "Reformation of American Administrative Law," at 1670. See also Thomas Merrill, "Capture Theory and the Courts: 1967-1983," *Chicago-Kent Law Review* 72 (1996-7), 1039-1117 (describing the 1967 – 1983 period as one of greater judicial scrutiny of agencies in an effort to maintain the goals of active state regulation in the face of greater skepticism of agency effectiveness and neutrality).

[44] *Office of Communications of United Church of Christ v. FCC*, 359 F.3d 995 (1966).

the aid and participation" of other representatives such as the church, community organizations, unions, and other such civil society groups actively participating in the regulatory process to convey their needs and interests. Simply relegating these citizen and advocacy groups to the mere practice of submitting letters and comments was insufficient. "While attracted by the potential contribution of widespread public interest and participation in improving the quality of broadcasting," the court continued, "the Commission rejects effective public participation by invoking the oft-expressed fear that a 'host of parties' will descend upon it and render its dockets 'clogged' and 'unworkable,'" but such a burden would ultimately be manageable.

Indeed, the Supreme Court briefly expanded the constitutional due process requirements for agency policymaking to require greater stakeholder participation within agency procedures. Traditionally, constitutional due process claims against agency procedures have been held to require the right to a hearing in adjudicatory proceedings,[45] but not requiring any further participatory rights for administrative rule-makings,[46] on the grounds that such participation was not feasible or desirable in a modern world marked by a large population of citizens and complex policymaking tasks that would be slowed down by a requirement that every affected citizen have a voice in the regulatory policy decision.[47] Yet in 1970, *Goldberg v. Kelly* briefly inaugurated a more robust regime of procedural due process protections, requiring a pre-termination hearing on top of other notice and

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[45] *Londoner v. City and County of Denver*, 210 U.S. 373 (1908).

[46] *Bi-Metallic Investment Co. v. State Board of Equalization*, 239 U.S. 441 (1915).

[47] *Bi-Metallic*, 239 U.S. at 445-46 (Holmes).

contestation procedures before an agency eliminated welfare benefits.[48] *Goldberg* expressed a concern not with administrative efficiency but with a deeper normative value of the "dignity and well-being of all persons."[49] This appeal to dignity justified both the welfare provisions themselves, as well as the right to an oral hearing.[50] But *Goldberg* lacked a well-defined theory of democratic accountability; indeed, the *Goldberg* majority was surprisingly hesitant to articulate exactly what a better procedural framework would look like.[51] Its core motivation, instead, was to prevent unjust state action by regulatory agencies. As with the APA before it, *Goldberg* was more indicative of a persisting anxiety over the power of regulatory agencies than it was of a particularly well-conceptualized response to that power.

Although lauded as a major breakthrough in assuring the citizen's participatory rights—as well as socioeconomic welfare benefits—for citizens, the *Goldberg* shift proved short-lived. The decision was criticized for creating undue administrative burdens and going beyond the textual scope of the Fourteenth Amendment,[52] culminating in an effective neutering of the procedural protections a few years later in *Mathews v. Eldridge*.[53] In *Mathews*, the Court argued that procedural protections would be justified only if they passed a three-part balancing test, weighing the private interest of the individual against the risk of erroneous

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[48] *Goldberg v. Kelly*, 397 U.S. 254 (1970).

[49] *Goldberg,* 397 U.S. at 264-65.

[50] *Goldberg,* 397 U.S. at 264-65.

[51] *Goldberg*, 397 U.S. at 268 ("We are not prepared to say that the seven-day notice currently provided by New York City is constitutionally insufficient per se.").

[52] See e.g. *Goldberg*, 397 U.S. at 271-78 (J. Black, dissenting).

[53] *Mathews v. Eldridge*, 424 U.S. 319 (1976).

deprivation of benefits, and the governmental interests—which for the *Mathews* court meant an examination of the administrative burdens and costs that greater procedural protections would entail.[54] Where *Goldberg*'s animating ethic was a focus on individual dignity, the *Mathews* court suggests a greater skepticism of both the importance of the welfare benefits themselves,[55] and the desirability of greater participatory engagement with agency decision-making. Indeed, like Holmes in *Bi-Metallic*, the *Mathews* majority exhibits an overwhelming concern with costly procedural protections undermining administrative efficiency, citing the already "elaborate character of the administrative procedures," and the existing "torpidity of the administrative review process."[56] The end result was a relatively rapid abandonment of the full potential of *Goldberg*'s Due Process holding; despite the concerns about unaccountable agency power, the expansion of due process rights seemed too inefficient, further bloating an already expansive and increasingly beleaguered regulatory state. As Horwitz comments, " one man's due process is another man's delay."[57]

Even advocates of such interest representation such as legal scholar Richard Stewart saw it as a failed policy, more likely to create gridlock and magnify the influence of sophisticated interests rather than creating genuine accountability and participation.[58] Courts, meanwhile, gradually eroded the doctrines they developed

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[54] *Mathews*, 424 U.S. at 335.

[55] See e.g. *Mathews*, 424 U.S. at 349-50 (J. Brennan, dissenting).

[56] *Mathews*, 424 U.S. at 342.

[57] Morton Horwitz, *The Transformation of American Law, 1870-1960* (New York: Oxford University Press, 1992), 246.

[58] Stewart, "Reformation of American Administrative Law," at 1670.

to bolster the procedural requirements for agencies to engage stakeholder groups.[59] The result has been a thinning out of procedural requirements, as agencies themselves are granted more leeway in choosing what procedures to use when formulating policies.[60]

More recently, scholars like Steven Croley[61] and Tino Cuellar[62] have suggested that a revamped administrative process can provide such a balance between engaging all affected interests while structuring political contest and voice with an eye towards regulation as problem-solving. For scholars in this vein, administrative process offers the potential for fostering a more balanced form of participation and voice that can make policymaking more publicly-interested even than legislation, by managing and structuring citizen engagement effectively.[63] A simple appeal to interest group pluralism by itself does not solve the challenges of facilitating collective action by diffuse and under-resourced groups.[64] Instead, agencies must proactively engage and consult all affected interests, for example through independent agency units specializing in structuring public consultation processes, or with officials who can act as "regulatory public defenders" tasked

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[59] See e.g., *Vermont Yankee Nuclear Power Corp. v. Natural Resources Defense Council*, 435 U.S. 519 (1978).

[60] *Seacoast Anti-Pollution League v. Costle*, 572 F.2d 872, cert. denied, (1978); *Chemical Waste Management Inc., v. USEPA*, 873 F.2d 1477 (D.C. Cir. 1989); *Heckler v. Campbell*, 461 U.S. 458 (1983).

[61] See Steven Croley, *Regulation and the Public Interests: The Possibility of Good Regulatory Government* (Princeton: Princeton University Press, 2008).

[62] Mariano-Florentino Cuellar, "Rethinking Regulatory Democracy," *Administrative Law Review* 57 (2005), 411-500.

[63] Croley, *Regulation and the Public Interests*, 134-41.

[64] Croley, *Regulation and the Public Interests*, 54-55.

with identifying and articulating the needs and views of affected but underrepresented groups.[65]

Collaborative governance

More recently, another group of scholars have argued for a turn to "collaborative governance," aiming to create a more participatory regulatory process that avoids the failures of the interest representation framework. This framework consists of several elements.[66] First, it focuses on collective problem-solving, where stakeholders are forced to articulate reasons, seek consensus, and find creative mutually beneficial solutions.[67] Second, this framework calls for a broad level of participation; the engagement of all interested and affected stakeholders is supported both for its epistemic value in bringing information to the policymaking process, and its normative value in fostering meaningful participation in the business of governance.[68] Third, the policies that result from these collaborative engagements between stakeholders and regulators are understood to be provisional, and experimental: through iterated interaction and discussion, regulators and stakeholders should be able to propose a range of policies that can be adapted over time, and tested in practice at the federal, state,

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[65] See Cuellar, "Rethinking Regulatory Democracy," 491-97.

[66] Orly Lobel, "The Renew Deal: The Fall of Regulation and the Rise of Governance in Contemporary Legal Thought," *Minnesota Law Review* 89 (2004), 342; Jody Freeman, "Collaborative Governance in the Administrative State," UCLA Law Review 45 (1997), 1-97; Michael Dorf and Charles Sabel "A Constitution of Democratic Experimentalism," *Columbia Law Review* 98 (1998), 267-473.

[67] Freeman "Collaborative Governance in the Administrative State," 23, Lobel, "The Renew Deal," 377.

[68] Freeman "Collaborative Governance in the Administrative State," 27, Lobel, "The Renew Deal," 373.

and local levels.[69] This same basic approach has also been advanced by other scholars under different rubrics, of "reflexive regulation", "experimentalism," or "pragmatist regulation".

For its advocates, this approach offers a more robust form of participation by all affected parties, recasting the regulatory process as one of collaborative problem-solving between groups of citizens who participate in all stages of regulatory policymaking, implementation, and revision, supplemented but not displaced by the expertise of regulators. In the process, citizens would expand their own capacities as problem-solvers, and regulation would be more of a bottom-up rather than top-down project of policymaking.[70] Such expansive participation provides multiple forms of accountability,[71] facilitates fluid and adaptive agency policymaking,[72] and fosters the long-term development of epistemically and normatively valuable participation.[73] This approach emphasizes collaboration between stakeholders and policymakers, in theory avoiding the dangers of deadlock by distributing responsibility for the policymaking process across the range of stakeholders and viewing policymaking as more than zero

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[69] See e.g. Dorf and Sabel, "A Constitution of Democratic Experimentalism"; Lobel, "The Renew Deal," 395-96.

[70] See e.g. Dorf and Sabel, "A Constitution of Democratic Experimentalism"; Christopher Ansell, *Pragmatist Democracy: Evolutionary Learning as Public Philosophy* (New York: Oxford University Press, 2011); Jack Knight and James Johnson, *The Priority of Democracy: Political Consequences of Pragmatism* (Princeton: Princeton University Press, 2011); Ian Ayres and John Braithwaite, *Responsive Regulation: Transcending the Deregulation Debate* (New York: Oxford University Press, 1992).

[71] Freeman, "Collaborative Governance in the Administrative State," 96

[72] Freeman, "Collaborative Governance in the Administrative State," 9-14

[73] Freeman, "Collaborative Governance in the Administrative State," 27, Lobel, "The Renew Deal," 384.

sum.[74] Further, instead of viewing agencies as reactive to an adversarial process of interest group bargaining, collaborative governance sees agencies as more dynamic, playing a role in fostering an ongoing dialogue over public policy.[75]

Regulatory agencies are critical to this vision of collaborative and experimentalist governance, because they function as conveners, guides, and capacity builders, providing the structure, resources, and benchmarks critical to facilitating productive and collaborative engagement between stakeholders.[76] They also serve as crucial focal points for citizens to mobilize around.[77] Indeed, under this framework the process of regulatory policymaking can be reformed to better encourage participation by a wide range of affected stakeholders beyond the more passive system of notice and comment contemporary rulemaking.[78] To the extent that other governmental bodies such as Congress or the courts are involved, their role is to support this collaborative and experimentalist policymaking process by providing financial resources, and external checks.[79]

Collaborative governance comes closest to articulating a theory of meaningful participation in the regulatory state. The biggest weakness of the collaborative governance framework, however, is its emphasis on consensus and its ultimately frictionless view of regulatory politics. The scholars writing in the

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[74] Freeman, "Collaborative Governance in the Administrative State," 5-6.

[75] Freeman, "Collaborative Governance in the Administrative State," 18-19.

[76] See Freeman, "Collaborative Governance in the Administrative State," 7, 31; Lobel, "The Renew Deal," 400, 457; Dorf and Sabel, "A Constitution of Democratic Experimentalism," 345-56.

[77] Ansell, *Pragmatist Democracy*, 144-6.

[78] See e.g. Cuellar, "Rethinking Regulatory Democracy," 491-97.

[79] Dorf and Sabel, "A Constitution of Democratic Experimentalism," 288-89.

collaborative governance framework all emphasize the pathologies of interest group pluralism as a foil for their arguments. While it is true that such cooperative engagement between stakeholders and regulators might be socially desirable, it seems unlikely that such regulatory policymaking can be sterilized of disagreement or contentiousness. But while these scholars are correct to point out the problems of political conflict and agency deadlock that arises out of the interest group pluralism framework, they ultimately conflate two distinct concepts. The problem with interest group pluralism framework is not the fact of political conflict *per se*; rather, its failures arise from a particularly toxic combination of political conflict with winner-take-all institutional structure where all interest groups must concentrate their energies at the initial policymaking moment. Because the stakes are so high, these groups are incentivized to begin push as hard as possible for their particular viewpoint. But rather than trying to sterilize policymaking of political conflict altogether—an impossibility outside of the world of theorizing—a compelling framework of democratic regulation should instead find ways to productively channel and contain such political disagreement. Indeed, this is the basic Madisonian insight: political disagreement is here to stay, and the task of institutional design to channel this disagreement in ways that are ultimately productive to society as a whole.

The collaborative governance framework is compelling not because of its emphasis on consensus, but rather because it provides a framework for understanding how political contest and democratic participation can be productively channel by looking beyond the initial moment of policymaking by the powerful regulator itself. As William Simon suggests, the most important element of the collaborative and experimentalist mode of regulation is its focus on enabling

citizens to directly experience the project of self-government, allowing for internal conflict but structuring it in a way that thickens the accountability and participatory capacity of citizens over time.[80] By suggesting ways in which groups can participate in debating policies, experimenting with them at local levels, and engaging in ongoing iterative debate, the collaborative governance framework suggests the way forward for a more productive form of democratic contest. The key seems to be to create conditions where policies can be initiated, evaluated, and then revised—and where citizens can be brought into the policymaking process, given the state, and thus encouraged to develop norms, knowledge, and capacities of self-government over time. This practice of experimentalism and ongoing engagement can be consistent with—and may even require—some degree of political disagreement to drive debate and innovation.

Towards a more democratic regulatory state

Though it purports to reconcile democratic self-rule with the modern regulatory state, contemporary administrative law falls short. Both the oversight and non-domination theories of regulation cast the regulatory state as an expression of the political agency of citizens. But they both ultimately position the citizen in a limited position, unable to actually contest or shape the exercise of regulatory authority. In the oversight theory, citizens can contest state policies, but they are positions far too upstream from the formulation and exercise of regulatory authority; contestation through elections is too removed from the actual

[80] William Simon, "New Governance Anxieties: A Deweyan Response," *Wisconsin Law Review* 727 (2010), 728-36.

practice of regulation and policymaking. In the non-domination theory, citizens are engaged more directly in the regulatory process but their role is limited and their actions filtered through a screen of expertise, and non-contestatory deliberative consultation.

Prevailing approaches in administrative law thus fall far short of this ideal of regulation as an expression of the political agency of citizens. Successfully articulating such a model may seem a Sisyphean task, one that administrative law will perennially grapple with. As Richard Stewart notes despondently in his seminal essay,

> The administrative state will abide, successfully resisting efforts to abolish it or reduce its operation entirely to market analogues. The only conceivable way out of the labyrinth would seem to be a new and comprehensive theory of government and law that would successfully reconcile our traditional ideals of formal justice, individual autonomy, and responsible mechanisms for collective choice, with the contemporary realities of decentralized, uncoordinated, discretionary exercises of governmental authority and substantial disparities in the cohesiveness and political power of private interests. Such a conception may well be unattainable, and in any event will not be achieved in the foreseeable future.[81]

There are, however, some potential resources for a richer democratic theory of regulation in administrative law. The efforts to expand the representation and participation of citizens within regulatory agencies suggest a set of tools that might be pressed into service of such a broader theory of democratic regulation. To overcome these limitations and reconcile regulation with democratic self-government, the next chapter suggests an alternative approach to democratic agency and institutions of economic governance.

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[81] Stewart, "Reformation," 1807.

7 DEMOCRATIC POLITICAL AGENCY

For Progressive Era reformers responding to the realities of a new industrial economy and the politics of Gilded Age America, the problem of democracy was primarily one of disparities in political power. Trusts, corporations, and party machines possessed a degree of political influence that was unrivalled, and almost certainly trumped the capacities of ordinary citizens. Today, similar concerns have animated recent efforts at democratic revival, whether in the form of Obama's 2008 campaign emphasizing civic engagement, or the appeal of left and right reform movements like Occupy and the Tea Party who shared a concern with the political power of big business and its impact on governmental policy. These concerns are not fundamentally about the grounds of democracy; rather they are about its practice. Whether we ground the value of democracy in claims of equal moral worth, epistemic value, or instrumental benefits to policymaking, growth, or other outcomes, democratic theories converge on a shared view that each citizen ought to possess an equal opportunity for political voice.[1] The anxieties of contemporary democracy stem from the intuition that such equal voice is far from a reality. This intuition is increasingly borne out in empirical studies highlighting the degree to which American political institutions are responsive not to the broad

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[1] Jack Knight and James Johnson, "What Sort of Political Equality Does Deliberative Democracy Require?," in James Bohman and William Rehg, *Deliberative Democracy: Essays on Reason and Politics* (Cambridge: MIT Press, 1997), 279-319.

range of citizens, but to particular demographics and especially to wealthier citizens.[2]

At the same time, unease over lay citizens' lack of knowledge and reasoned judgment motivates the turn to elite decision-makers, experts, or markets. All seem to offer a more dependable and socially-optimal mode of making collective judgments free of irrationality, passion, or tumult. Indeed, defenders of the regulatory state present it as a way to meet both concerns: on the one hand, it sterilizes policymaking of the ignorance, partiality, and corruption of democratic politics; on the other hand, it claims to further the ideal of self-government by pursuing the common good as refined through elected officials and delegated expert authority. But as the persisting anxieties over technocratic governance suggest, this resolution leaves much to be desired.

This chapter draws inspiration from the radical democratic voices of the Progressive Era, especially John Dewey and Louis Brandeis. For these thinkers, the problem of markets and economic upheaval demanded a specifically *democratic* response, where new institutions had to be devised to unlock the agency and capacities of citizens to address these economic concerns themselves. This democratic ethic of economic governance represents a very different tradition from the technocratic inheritance through the New Deal and in contemporary economic policy debates.

The technocratic view, as suggested in previous chapters, suggests economic governance be addressed through institutions that are centralized, expert-led, and

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[2] See e.g., Martin Gilens, *Affluence and Influence: Economic Inequality and Political Power in America* (Princeton: Princeton University Press, 2012); Larry Bartels, *Unequal Democracy: The Political Economy of the New Gilded Age* (Princeton: Princeton University Press, 2010).

which pursue policies aimed at managing and optimizing the market. By contrast, in this chapter, I develop a democratic conceptualization of economic governance. I argue below that we should embrace the promise of regulation as an expression of the political agency of the public to address the kinds of concerns that arise in the modern market economy, such as from the threats of private or market power. But to make this promise a reality, we must change how we think about both "democracy" and "regulation" as concepts. I suggest below a normative rethinking of democracy not just as a matter of input or voice, but as a matter of experience in governing. This in turn suggests a revised understanding of regulation as forums and spaces where such experience is fostered, catalyzed, and housed.

First, citizens must have access to the actual exercises of political power through mechanisms assuring representation or participation. Rather than relying on experts who can engage citizens on an ad hoc basis, and who exercise authority under the overview and directives of elected officials, we must reconstitute regulatory institutions as forums for citizens to engage in active and direct experience with the challenges and tensions of governing.

Second, these governing institutions must themselves be reorganized to serve as forums for democratic action. These institutions must be sufficiently consolidated and visible such that citizens can organize around them, targeting their claims to these institutions. But these institutions must also possess sufficient powers to respond to these citizen claims.

Third, citizens must be able to contest matters of public policy on moral, not just technical, grounds. Economic policy implicates moral and political judgments. Submerging these considerations under a veneer of technical problem-

solving not only mis-describes the issues at stake, it also narrows the scope for democratic agency on the part of non-experts.

Democracy and regulation as experience

In a democratic society, citizens are not just bearers of preferences or sources of information. They are—or ought to be—co-authors of government. In light of the reach, size, and complexity of modern governance, however, such self-governance has been most conventionally achieved through indirect modes of political power, where citizens sanction the workings of government pursued through the authority delegated to representatives and experts. Direct democracy through mass referenda, by contrast, seems ineffectual in such a complex environment. But the failures of contemporary democracy are the results of a particularly emaciated set of democratic institutions and practices.

In laissez-faire and technocratic economic governance, these pathologies of democratic disagreement, conflict, corruption, and ignorance are resolved by sterilizing, limiting, and screening democratic activity away from the actual work of policymaking; these systems place their faith for economic order in apolitical markets or neutral experts. By contrast a more democratic approach rests its faith on the capacity of citizens to learn over time, to forge common solutions when presented with actual problems that they experience and for which they are ultimately responsible. *Expanding* rather than limiting citizens capacities so that they experience *both* the challenges of governing *and* the repercussions of their actions thus offers an alternative to either markets or experts. Such direct experience with governance will not transform democratic citizens into consensus-

seeking rational policy experts. Democratic politics will remain conflictual, messy, chaotic. But it provides a means through which disagreements can be mediated and judgment developed.

How can citizens, placed in such a central role, actually govern effectively? A standard response from democratic theory suggests the role of civic virtue: citizens must be educated, must engage in good faith and rational discourse. But this turn to individual virtue is misleading, implicitly rooted in a declining faith in the viability of political engagement at the macro institutional level.[3] The capacity for political agency is primarily is not only a product of individual qualities, but rather is dynamically generated under particular social and institutional contexts that enable effective political functioning.[4] Institutions are vital for creating the spaces in which citizens can partake in meaningful participation in the project of governance. Institutional structure is crucial to empower citizens and facilitate contestation and participation in ways that are productive and effective.[5]

Absent such institutional support to foster effective and meaningful democratic engagement, it is no wonder that democratic politics seems

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[3] Iris Young, *Responsibility for Justice* (New York: Oxford University Press, 2011), 40.

[4] See e.g., James Bohman, "Deliberative Democracy and Effective Social Freedom: Capabilities, Resources, and Opportunities," in Bohman and Rehg eds., 321-48. As Dana Villa notes, sustaining citizen engagement with politics requires that we "care for the public world," that we "create and preserve a set of laws, institutions, and public spaces that make active citizenship possible." Dana Villa, *Public Freedom* (Princeton: Princeton University Press, 2008), 347. As Melvin Rogers notes, "to the extent that government institutions are complicit in this process of political alienation and domination, citizens are well within their right to rethink the purpose and boundaries of those institutions." Melvin Rogers, "Democracy, Elites, and Power: John Dewey Reconsidered," *Contemporary Political Theory* 8:1 (2009), 68-89, at 87.

[5] See e.g. Charles Beitz, *Political Equality* (Princeton: Princeton University Press, 1990), 98 ("Popular participation in political decisions is possible only within an institutional framework that organizes and regulates it"). See also Carole Pateman, "Participatory Democracy Revisited," *Perspectives on Politics* 10:1 (2012), 7-19, at 10 (The "capacities, skills, and characteristics of individuals are interrelated with forms of authority structures").

unproductive and ineffective. Meaningful democratic agency can only be realized when citizens are put in positions of engaging in the actual practice of governing: judging alternatives, weighing tradeoffs, living with the results of these decisions—not as a lone moment of citizen engagement but as an ongoing practice through which we as citizens develop knowledge, judgment, and experience. It is here that the institutions of regulation arise not as a threat to democratic vitality, but as a potential *site* for democratic political agency.

There is a growing literature on how institutional innovations can foster effective citizen roles in governing placing citizens alongside experts, from citizen's juries, to participatory budgeting, to deliberative polling.[6] But these accounts have yet to produce a more systematic theory of the principles of institutionalizing democratic agency that can scale up. Many of these innovations focus too much on seeking consensus and ensuring rational deliberation, but the real value of these small-scale deliberative experiments lies not in their attempt to foster consensus or deliberation, but rather in the degree to which these practices create *regular institutions for empowered participation*.[7] A more systematic institutionalization of citizen agency must focus on this contestatory view of catalyzing and channeling the mobilization of citizens. This in turn points to a very different view of the regulatory state.

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[6] See e.g., James Fishkin, *When the People Speak: Deliberative Democracy and Public Consultation* (New York: Oxford University Press, 2011); Archon Fung, *Empowered Participation: Reinventing Urban Democracy* (Princeton: Princeton University Press, 2006); Gianpaolo Baiocchi, Patrick Heller, and Marcelo K. Silva, *Bootstrapping Democracy: Transforming Local Governance and Civil Society in Brazil* (Palo Alto: Stanford University Press, 2011); Archon Fung, "Reinventing Democracy in Latin America," *Perspectives on Politics* 9:4 (2011), 857-871.

[7] Pateman, "Participatory Democracy Revisited," 8.

Where technocratic Progressives like Landis or Sunstein cast the regulatory state as a space for cultivating expert-led rational deliberation over public policy, these institutions can be reformulated to act as spaces in which citizens can experience the demands and difficulties of governance, where they can learn judgment and exercise meaningful political agency. As Elizabeth Anderson notes, democracy depends on "the social conditions of autonomy people need to articulate, change, and promote their own values in ways they can reflectively endorse."[8] As institutions tasked with the development and implementation of specific policies, regulatory agencies can serve as a unique "nexus of democracy and governance," creating spaces for citizens to engage directly in policy formulation and implementation in a way that is difficult in context of traditional democratic institutions of elections and legislatures.[9] Through the political and cooperative project of regulation, citizens reshape the workings of the economy.[10] Part of this is out of necessity: the realities of regulatory policymaking are that substantive moral and political judgments have to take place in the regulatory process. The ends specified by legislatures are necessarily broad and vague, and not all disagreements can be worked out in the traditional elected branches.[11] There will always be moral judgments to be made by those institutions charged with

[8] Elizabeth Anderson, *Value in Ethics and Economics* (Cambridge: Harvard University Press, 1993), 211.

[9] See Chris Ansell, *Pragmatist Democracy: Evolutionary Learning as Public Philosophy* (New York: Oxford University Press, 2011), 3-4. See also Mark Warren, "Governance-Driven Democratization," *Critical Policy Studies* 3:1 (April 2009), 3-13.

[10] See e.g. Joseph Heath, "The Benefits of Cooperation," *Philosophy and Public Affairs* 34:4 (2006), 313-351, making a similar argument about reconceiving the welfare state as a constructive realization of a socially desirable form of cooperation, rather than as merely a residual response to the market economy.

[11] Henry Richardson, *Democratic Autonomy: Public Reasoning About the Ends of Policy* (New York: Oxford University Press 2002), 13.

devising the final end result policies and implementing them. These judgments cannot be sidestepped through expertise.[12]

But the democratic potential of regulation is not just a product of necessity in specifying public policy. Regulatory institutions—those governmental bodies charged with formulating and implementing final policies—have affirmative civic value as spaces where citizens can experience the tasks of policymaking. We conventionally understand "regulation" as the technical implementation that follows legislation and elections, which serve as the primary sites of democracy. But instead we ought to understand regulation broadly, not as the technical implementation of legislative directives, but as the practice of governance where broad principles and goals are translated into actual policies, implemented, and carried out. On this understanding, "regulation" encompasses not only centralized federal agencies like the SEC, which develop and implement national policies that craft and implement regulations, but also local level bodies like municipalities, which constitute a second key domain where the practice of governance meets the "front-line" of implementation and affecting citizens. Viewing regulations as a site of democratic agency thus broadens our scope of what regulatory institutions do, and what kinds of institutions—national and local—count as potential sites for democratic governance.

But how should these institutions be reformed to fulfill this promise? Inspired by the thought of Dewey and Brandeis, the rest of this chapter outlines several conditions for such citizen empowerment. In particular, there are three key conditions for democratic agency. First, citizens must be empowered to participate

[12] See Richardson, *Democratic Autonomy*, 114-129.

in economic decision-making alongside experts. Second, citizens require institutional forums to house and catalyze political action. These forums provide a focal point against which citizens can organize, mobilize, and make claims. The existence of these institutions thus enables citizens to act on the kinds of diffuse and systematic challenges that otherwise would be beyond any one individual or group's reach. But at the same time, these institutions must have the capacities and powers to respond to the claims raised by citizens effectively. Weak regulatory bodies do little to sustain citizen action for without the likelihood of an effective response, political engagement is less worthwhile. Third, the content of the issues in question must be understood in moralized, rather than technical or depoliticized terms. Without moral stakes, it is difficult to catalyze and enable meaningful citizen action. Citizens must therefore be empowered to contest economic policies along their moral and political dimensions.

Participation, representation, and expertise

In the midst of Progressive Era reform movements from issues of antitrust, corporate power, and financial panics, both Dewey and Brandeis argued for a specifically democratic approach to these economic issues, where citizens where empowered as the key drivers of state action. For both thinkers, an active and engaged citizenry did not necessarily mean a rejection of representatives and experts; rather, democracy would require that representatives and experts operate in ways to facilitate rather than supplant the political agency of citizens.

Representation could help citizens mobilize and magnify citizen voice. Dewey argued that through representative political associations, individually

disempowered citizens could to educate themselves, coordinate action, to develop political power.[13] Brandeis emphasized the importance of citizen mobilization through trade unions and other groups as a form of countervailing power against monopolies and corporations.[14] Once organized through such associations, citizens would be better equipped to counteract the excesses of private power, assert their own interests, and engage with the policymaking process. Such political association would improve the representation of different social groups in decision-making within firms and in governments, check abuses of private power, and direct the state to regulate the market economy. Thus, Brandies advocated worker representation and collective bargaining with firms as a way of balancing representation within corporations to check the exercise of private corporate power.[15]

Similarly, citizen action had to operate alongside, rather than being displaced by, expertise. Because the administrative burden of fully regulating the market economy was beyond the scope of any possible commission or set of experts,[16] Brandeis argued that such regulation would have to proceed through the iterative and ultimately democratic process of policy experimentation, where citizens could propose particular regulatory schemes, and then revise them based

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[13] John Dewey, *Public and Its Problems* (Athens: Swallow Press, Ohio University Press, 2004), 138-142.

[14] See e.g. Brandeis, "How far have we come on the road to industrial democracy? An interview," in Osmond Fraenkel, ed., *The Curse of Bigness: Miscellaneous Papers of Louis Brandeis* (New York: Viking Press, 1935), 43-7; "Efficiency Systems and Labor," in Fraenkel, ed., *Curse of Bigness*, 48-50; "On Industrial Relations," in Fraenkel, ed., *Curse of Bigness*, 70-95, at 79. See also Philippa Strum, ed., *Brandeis on Democracy* (Kansas: University Press of Kansas, 1995), 74-78.

[15] See Brandeis, "On Industrial Relations," in Fraenkel, ed., *Curse of Bigness*, 76, 79.

[16] Brandeis, "Competition"(1913), in Fraenkel, ed., *Curse of Bigness*, 112-24.

on experience. Brandeis saw regulation not as a technocratic system, but rather as a democratic one where citizen participation was integrated with the knowledge of experts—in contrast to the valorization of expertise articulated by many other Progressives. As Gerald Berk argues, while Brandeis shared the Progressive "commitment to applied science, state building, wealth redistribution, trade unionism, and the welfare state," he ultimately thought these other Progressives "reified economic power, overestimated the ability of science to overcome human fallibility in government and the economy, and underestimated the capacity of common people to achieve public ends."[17] Despite his admiration of the new techniques of expertise and "scientific management," Brandeis routinely argued for the linking of labor representatives alongside expert policymakers in the making of trade, antitrust, and workplace regulations.[18]

Dewey theorized this interaction between citizens and experts somewhat more broadly than Brandeis, but he shared this intuition that effective and democratic policymaking required citizens to work alongside experts. While Dewey agreed with other Progressives such as Walter Lippman that professional expertise was needed to develop effective public policies, he argued that such expertise had to be integrated with democratic engagement. Experts did indeed possess factual knowledge that was vital to effective policymaking, but it is "impossible" for such experts to "secure a monopoly of such knowledge as must be used for the regulation of common affairs."[19] "A class of experts," argued

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[17] Gerald Berk, *Louis D. Brandeis and the Making of Regulated Competition, 1900-1932* (New York: Cambridge University Press, 2009), 88.

[18] See e.g., Brandeis, "Efficiency Systems and Labor," in Fraenkel, ed., *Curse of Bigness*, 48-50.

[19] Dewey, *Public and Its Problems*, 206.

Dewey, "is inevitably so removed from common interests as to become a class with private interests and private knowledge, which in social matters is not knowledge at all."[20] In an argument akin to later defenses of the market as a mode of aggregating diffuse knowledge and information in society,[21] Dewey argued that local knowledge of lay citizens was crucial both to defining social problems and in evaluating the effectiveness of policy responses.[22] Such participation was also crucial to keeping policymakers themselves accountable. "No government by experts in which the masses do not have the chance to inform the experts," argued Dewey, "will be anything but an oligarchy in the interests of a few."[23] Expert policymakers therefore had to be embedded in political debate, discussion, and persuasion—in short, in democratic politics—where citizens could express their needs, values, and interests, and judging whether policy outcomes fulfilled those aspirations.[24] Through such empowered participation alongside experts, citizens would become more knowledgeable and capable over time; the current limits to citizen capacities were products of their institutional position in governance, rather than an intrinsic failure on the part of lay persons.[25]

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[20] Dewey, *Public and Its Problems*, 207.

[21] See e.g., John Tomasi, *Free Market Fairness* (Princeton: Princeton University Press, 2012).

[22] See also Rogers, "Democracy, Elites, and Power," 73-80. "Where decision-making is based less on the continuous input from public hearings, town hall meetings, advisory councils and other deliberative bodies there is greater reason to be concerned about the ends to which those decisions aim."

[23] Dewey, *Public and Its Problems*, 208.

[24] Dewey, *Public and Its Problems*, 208-209. See also Rogers, "Democracy, Elites, and Power": "Where decision-making is based less on the continuous input from public hearings, town hall meetings, advisory councils and other deliberative bodies there is greater reason to be concerned about the ends to which those decisions aim."

[25] Dewey, "Public Opinion," *The New Republic*, May 3, 1922; "Practical Democracy," *The New Republic*, December 2, 1925.

These views of Dewey and Brandeis are instructive. Thickening citizens' experience of governing does not necessarily require pure direct democracy. But it does require inverting the relationship between citizens and elite government officials—representatives and experts. Where today both representatives and experts exercise political agency as the main decision-makers sanctioned by a mostly passive citizenry, these offices should instead function as advisors and supporters, not displacers, of citizen agency. As Carole Pateman argues, "it is only if the individual has the opportunity directly to participate in decision making that, under modern conditions, he can hope to have any real control over the course of his life or the development of the environment in which he lives."[26] Rather than deferring or delegating authority to these elite individuals on the grounds that they possess better judgment, citizens would, in this view, develop their own capacities for judgment over time, through the ongoing experience with the difficulties, challenges, and reversals of governing.

So long as representatives are seen as either purely transmissive of public opinion, or overly powerful appointed rulers, the scope for political contest, fluidity, and responsiveness is closed off.[27] This problem of elite rule can be resolved by expanding the ability of citizens to contest political elites and participate in the ongoing and day-to-day routines of policy and politics.[28] Under this approach, representation must be understood not as a delegation of

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[26] Carole Pateman, *Participation and Democratic Theory* (New York: Cambridge University Press, 1970), 110.

[27] See e.g. Hannah Arendt, *On Revolution* (New York: Penguin, 2006), 229.

[28] See e.g. Melvin Rogers, "Democracy, Elites, and Power: John Dewey Reconsidered," *Contemporary Political Theory*, 8:1, 68-89, at 81-2.

responsibility and action from a now-passive citizenry, but instead as embedded in and catalytic of ongoing political contest.[29] Representatives articulate positions that help engage, mobilize, and educate their constituents, while constituents themselves shape the views and actions of their representatives through such mobilization.

Similarly, experts should not be abandoned, but nor should they trump democratic judgment. Rather, the role of expertise must be subordinated to democratic contest. Experts can provide information, advice, and knowledge as inputs into democratic debate, but it is this democratic debate that must hold sway to check, guide, and channel the use of expert knowledge. In contrast to the technocratic celebration of experts as operating apart from ordinary politics, experts are not simply neutral purveyors of fact. Experts are partly political agents whose conceptualizations and arguments help shape and create social world.[30] Further, expert accounts of social matters especially such as economic policy are intertwined with normative as well as factual understandings.[31] The judgments of

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[29] Lisa Disch, "Toward a Mobilizational Conception of Democratic Representation," *American Political Science Review* 105:1 (Feb 2011), 100-114. As Hannah Pitkin argues in her classic study of representation, even the ideal of representation ultimately hinges on some form of democratic empowerment: "we show a government to be representative not by demonstrating its control over its subjects but just the reverse, by demonstrating that its subjects have control over what it does." Hannah Pitkin, *The Concept of Representation* (Berkeley: University of California Press, 1972), 232.

[30] David Kennedy, "Challenging Expert Rule: The Politics of Global Governance," *Sydney Journal of International Law* 27 (2005), 5-28. See also Peter Hall, "Policy Paradigms, Social Learning, and the State: The Case of Economic Policymaking in Britain," *Comparative Politics* 25:3 (1993), 275-296, at 279 ("policymakers customarily work within a framework of ideas and standards that specifies not only the goals of policy and the kind of instruments that can be used to attain them, but also the very nature of the problems they are meant to be addressing").

[31] See e.g. Charles Taylor, "Neutrality in Political Science," in *Philosophy, Politics and Society*, Third Series, Peter Laslett and W. G. Runciman, eds. (Oxford: Blackwell, 1967), 25-57; Elizabeth Anderson and Richard Pildes, "Slinging Arrows At Democracy: Social Choice Theory, Pluralism, and Democratic Politics," *Columbia Law Review* 90 (1990), 2121-2214.

experts must therefore be subject to broader political judgment by citizens. Such ongoing citizen engagement is crucial to ensuring expertise is directed to collectively chosen ends and the normative dimensions of policy choices are assessed as such.[32] Experts may still contribute vital knowledge to policy debates, but democratic citizens must have a broader role than commonly recognized in determining the political implications of those expert findings.[33]

Regulatory institutions as forums

The idea of democratizing the exercise of state policy through greater representation and participation of citizens is a familiar one in participatory democratic theory. But it is less commonly noted that providing citizens with such access to decision-making bodies by itself is not enough to achieve meaningful democratic agency. The democratic potential and value of such participatory access also depends on the broader institutional and discursive context in which such participation takes place. A key enabling condition for democratic agency, then, is the very creation of institutional forums that are readily visible as clear targets for citizen mobilization and action, and easily accessible.

The presence of such forums is especially significant in context of economic governance. The substantive challenges of modern social and economic order too often are of a structural or diffused nature that makes them seem as beyond the

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[32] Elizabeth Anderson, "Epistemology of Democracy," *Episteme* 1:2 (2006), 8-22. See also Rogers, "Democracy, Elites, and Power," 79 ("Where decision-making is based less on the continuous input from public hearings, town hall meetings, advisory councils and other deliberative bodies there is greater reason to be concerned about the ends to which those decisions aim.")

[33] Harry Collins and Robert Evans, *Rethinking Expertise* (Chicago: University of Chicago Press, 2007), at 115-26, 138-9.

scope of individual agency. This is particularly a challenge for structural forms of injustice or acting to alter diffused systems such as markets or other aggregated social processes that create forms of domination or narrowed capacities for some, and greater capacities for others.[34] In these settings, "individuals experience social structures as constraining, objectified, thing-like," constraining the terrain of possibility.[35] Institutions of government provide "mediated instruments for the coordinated action" of citizens implicated in and troubled by these macro structures.[36] This suggests that state institutions are critical in rendering structural and diffuses dynamics subject to human agency.

Regulatory institutions as consolidated targets for mobilization

In his attempt to theorize the conditions for democratic agency, Dewey suggested the importance of state institutions as focal points for political action. Without these institutions, it would be difficult for citizens to organize, mobilize, and know where to target their claims.

The problem of the modern economy, for Dewey, was primarily one of political institutions: the threats that market forces and private power posed to individual and collective well-being were pernicious because they appeared beyond the scope of individual agency. Individuals in the modern economy, Dewey wrote, was the individuals felt disempowered and "paralyzed," "caught in the sweep of

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[34] Young, *Responsibility for Justice*, 52. Structural injustice "exists when social processes put large groups of persons under systematic threat of domination or deprivation of the means to develop and exercise their capacities, at the same time that these processes enable others to dominate or to have a wide range of opportunities for developing and exercising capacities available to them."

[35] Young, *Responsibility for Justice*, 53.

[36] Young, *Responsibility for Justice*, 112.

forces too vast to understand or master."[37] This political disempowerment was inequitably distributed across society; too often, powerful vested interests such as business corporations possessed sufficient technical expertise, knowledge, and power to engage in political action, while ordinary citizens did not.[38] The failures of democratic politics—citizen apathy, disproportionate political power among business and wealthy interests, alienation of citizens from politics, and prevalence of machine party politics and factional bargaining—stemmed from the fact that existing routes for democratic action—parties and representative electoral democracy—were incapable of effectively organizing the "inchoate and amorphous" public into a form capable of "effective political action relevant to present social needs and opportunities."[39] As a result, "the prime difficulty" for Dewey was "discovering the means by which scattered, mobile in manifold public may still recognize itself as to define and express its interests."[40]

Given the challenges of overcoming structural challenges of the market and concentrated private power, individuals required political institutions to facilitate their very capacity to respond to these problems of the economy. State institutions for Dewey served a dual purpose: in addition to making and implementing policies, these institutions were also key "structures which catalyze action," providing a "mechanism for securing to an idea [the] channels of effective action."[41] State institutions offered a mechanism for citizens to organize and take action on issues

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[37] John Dewey, *Public and Its Problems* (Athens: Swallow Press, Ohio University Press, 2004), 135.

[38] Dewey, *Public and Its Problems*, 136.

[39] Dewey, *Public and Its Problems*, 125.

[40] Dewey, *Public and its Problems*, 146.

[41] Dewey, *Public and Its Problems*, 54, 143.

that otherwise would be so diffuse in effect and consequences that they would pose difficulties to resolve on an individual basis. As such, the state was critical to facilitating genuine democratic self-rule—and particularly for enabling citizens to take control over market dynamics which would otherwise be too diffused and decentralized to be reshaped on the basis of apolitical individual action alone.

Dewey's sketch points to an important condition for democratic agency today. To be effective political agents, citizens require institutions that can help focus and coordinate mobilization. Thus, for regulatory institutions to act as viable forums for participation, they must be sufficiently visible and empowered to act as *focal points* for meaningful engagement by citizens, targets against which citizens can mobilize or make claims. Unless these institutions are visible with clear authority and responsibility for a given set of issues, it is difficult for citizens to mobilize and know whom to address. While sophisticated interests can navigate a confusing ecology of fragmented and submerged authorities, equal democratic voice is fostered by the presence of clear targets for citizen engagement.

Sometimes this requirement can be discharged by geographically-based jurisdictions, such as legislative districts, cities, and states. But often, particularly in expansive issues such as economic policy, the range of interests will be diffuse and national, requiring a topically-focused rather than geographically-focused policymaking institution. Rather than relying on geographically-determined districts as in legislative elections, agencies can be designed in a more variegated fashion, facilitating the mobilization and empowerment of different 'publics'—for example, those affected by environmental concerns who would engage with the Environmental Protection Agency; those from the small business sector engaging with the Small Business Administration, and the like. Regulatory agencies thus

have the "capacity to bring into existence dynamic, serial, and overlapping peoples and constituencies based on the 'all affected' principle in contrast to pre-defined and relatively static territorial constituencies," defining constituencies not through region and territory but through who actually possesses a stake in the issue in question.[42]

At the same time, these institutions must also have sufficiently broad *powers* to be able to respond to citizen concerns. The very motivation to engage in political participation requires that individuals feel a "sense of political efficacy."[43] While many democratic theories emphasize the need to resist exercises of power, "simply blocking the exercise of power is often a bad solution;" instead modern democracy "needs more collective power to solve the growing number of collective action problems."[44] Thus, participation in weak, fragmented, or submerged regulatory bodies is not efficacious or valuable, since these institutions are either difficult to identify and mobilize around, or are too incapacitated to actually respond to the concerns that citizens may voice, or both. The idea of target and capacity suggest civic benefits to consolidated, powerful regulatory bodies.

Multiplying democratic forums

Another way to promote democratic agency is through the multiplication of such institutional sites for citizens to target and in which citizens can experience

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[42] Warren, "Governance-Driven Democratization,"6.

[43] Pateman, *Participation and Democratic Theory*, 46.

[44] Jane Mansbridge, "On the Importance of Getting Things Done," *Political Science and Politics* 45:1 (2012), 1-8; at 5.

the demands of governance. This view cuts against traditional calls for decentralization as a way to limit state power; to function as effective spaces for democratic action, these forums must retain broad authority. But this view also challenges traditional calls for centralized authority which also tends to seek uniformity. In their place, this approach to democratic forums would create multiple sites, *each of which* possess broad authority to act. The result would be to provide more—and more accessible—spaces for democratic action.

The value of this commitment to multiple democratic spaces is nicely captured by Brandeis' arguments for decentralization. Brandeis is traditionally seen as a defender of localism, federalism, and decentralization, in contrast to the centralizing tendencies of the New Deal. Indeed, Brandeis often invoked the tradition of police power to justify state-level experiments with policies aimed at addressing economic upheaval, from minimum wages to regulations of corporations.[45] But at root, Brandeis' turn to states was not a celebration of states so much as it was a search for *instruments* through which citizen agency could be fostered. As such, his account carries valuable insights for the creation of institutions today that can similarly provide spaces for meaningful democratic agency, whether at the local or national level.

Brandeis saw the problem of economic governance as requiring not the elevation of insulated expert managers, but rather the creation of spaces where citizens could experience meaningful political power, overcoming the challenges of the changing economy through their own experimentation and political judgment.

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[45] See Louis Brandeis, "The Constitution and the Minimum Wage," in Fraenkel, ed., *The Curse of Bigness*, 52-69.

In *Liggett v. Lee* (1932),[46] the Supreme Court struck down a Florida state law designed to limit the spread of newly-emerging chain stores such as A&P by imposing a graduated tax on chain stores that would increase with the number of branches the store had in the state. Brandeis dissented, arguing in favor of upholding the Florida law, less out of a defense of state sovereignty, and more out of a concern about tackling the growing private power of large corporations through mobilized democratic action.

Brandeis opens by arguing that corporate privileges are a matter of state policy, granted or limited to promote the state's public ends.[47] The historical fear of corporations—a "fear of encroachment upon the liberties and opportunities of the individual… of the subjection of labor to capital…of monopoly"—had animated prior waves of social reform and public policy, through traditional limits on corporate power such as legal constraints on capital stock, corporate powers, and corporate size.[48] These limits, however, had gradually eroded out of concern by states that corporations would simply circumvent local regulations.[49] Florida's legislation was valuable not necessarily as an expression of Florida's intrinsic sovereign authority, but rather as a tool in the "struggle to preserve" independent retailers against the power of large corporate chains "menacing the public welfare."[50] Indeed, this struggle was more than simply a matter of political

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[46] *Liggett v. Lee*, 283 U.S. 517 (1932) (J. Brandeis, dissenting).

[47] *Liggett,* 283 U.S., 545.

[48] *Liggett,* 283 U.S., 548; 550-7.

[49] *Liggett,* 283 U.S., 557.

[50] *Liggett,* 283 U.S., 568, 569.

convenience or efficiency; rather it was tied to a deeper moral commitment to an egalitarian and democratic economy. Thus Florida's legislators

> may have believed that the chain store, by furthering the concentration of wealth and of power and by promoting absentee ownership, is thwarting American ideals; that it is making impossible equality of opportunity; that it is concerning independent tradesmen into clerks; and that it is sapping the resources, the vigor and the hope of the smaller cities and towns.[51]

Given this matter of public concern, the state of Florida, in Brandeis' view, was well within its rights to impose a tax that fell differentially on different chain stores at different levels: the "state may prohibit a business found to be noxious and, likewise, may prohibit incidents or excrescences of a business otherwise beneficent."[52] For those concerned that states may abuse such authority, Brandeis argued that such power was grounded in the democratic will of citizens. Therefore, such exercises of power would be legitimate. More importantly, they would foster the capacities of ordinary citizens to continue to govern and reshape their own social and economic destinies. "Only through participation by the many in the responsibilities and determinations of business," wrote Brandeis, "can Americans secure the moral and intellectual development which is essential to the maintenance of liberty."[53] By arguing for the power of the state of Florida to "give it [the public will] effect and prevent domination in intrastate commerce by subjecting corporate chains to discriminatory license fees," Brandeis sought to ensure that "citizens of each state are still masters of their destiny."[54]

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[51] *Liggett,* 283 U.S., 568-9.

[52] *Liggett,* 283 U.S., 574.

[53] *Liggett,* 283 U.S., 580.

[54] *Liggett,* 283 U.S., 580.

Brandeis' defense of local spaces is instructive, for it highlights the importance of ensuring not just one national forum for political action, but rather multiple such spaces, particularly at the local level. Each of these spaces would still have to possess the features described above—participatory access, clear targets for citizen action, sufficient powers to respond to claims. But multiplying these spaces creates more ready access of citizens to a forum for experiencing political agency.

Balancing consolidation and multiplication of spaces

These multiple objectives—creating a sufficiently powerful forum to focus citizen action and respond to it, while also remaining accessible to the citizens themselves—suggest the importance of balancing between centralization of regulatory authority in few, powerful bodies on the one hand, and multiplying regulatory spaces to be closer to more localities and communities on the other. Institutional consolidation has some civic democratic benefits—by centralizing the debate and power in one arena, it becomes easier for would-be participants to identify (worthwhile) targets against which to make claims and specific institutions to hold accountable for policy failures. The consolidation ethic also promises consistency and a certain kind of stability. But these benefits come at the risk of creating a high-stakes political dynamic that inhibits innovation and experimentation, while narrowing the capacity of many to participate in the process, as not all citizens or groups are equally capable of engaging in policy debate at the federal level. Decentralization, meanwhile, allows for a multiplying of public spaces, creating more opportunities for empowered engagement, and creating spaces where views that are defeated elsewhere may find refuge and

expression. This facilitates experimentation and wider participation. Yet to the extreme, such fragmentation can make it difficult to hold on to substantive gains achieved elsewhere, or can create a chaotic public terrain such that it becomes even harder for individuals and groups to mobilize and engage—if there are too many equally salient public arenas, how are participants to know let alone choose where to stake their claim? Such confusion and dissipation of mobilizational energies favors more sophisticated and well-resourced interest groups.

These considerations suggest changes to 'horizontal' divisions of policymaking authority between regulatory agencies. As with the problem of decentralization, the multiplication of specialized regulatory agencies works to dissipate the abilities of many countervailing groups and associations to engage, while powerful interest groups are likely to manipulate such divisions to their advantage. Thus, splitting state authority across different agencies all of which have some degree of responsibility for a topical area of policy creates similar challenges for democratic participation. On the one hand, different agencies may be more accessible to different interest groups. But on the other hand, such a regulatory patchwork creates a policymaking ecology where all but the most sophisticated players are left in the dark as to which agency they should engage to respond to a particular problem. Instead, we must reconsider the proliferation of federal regulatory agencies. There is a civic benefit that is often overlooked to consolidating and centralizing regulatory authority in ways that make the relevant policymakers more readily visible to and contestable by citizens—rather than being hidden within a confusing cacophony of competing and overlapping regulatory bodies, a complexity that not only frustrates citizen agency but also creates

multiple opportunities for more sophisticated parties to lobby, influence, and manipulate the regulatory process.

These considerations also suggest a different approach to 'vertical' forms of decentralization: specifically, the question of local power in a complex political order. Localities are often hamstrung in their policymaking capacities, hemmed in by state limits on local power and deep unease about local partiality, corruption, and policy incoherence. Instead, we must revive the viability of the locality as a space for democratic mobilization and effective policymaking. This in turn requires reconceptualizing familiar discourses of decentralization and localism. Traditionally, we are accustomed to understanding localism in terms of "local autonomy"—the freedom for a locality to make whatever policies it sees fit. This necessarily creates an anxiety for those instances where localities abuse their autonomy, for example to violate civil rights or basic liberties. This conventional view also suggests major efficiency losses to having localities pursue their own autonomous policies, creating the specter of a "patchwork" of regulations that undermine the efficiency of regional, national, and international economic and social activity. But instead of a zero-sum opposition between local autonomy (and potential corruption), and national uniformity, the goal of democratic agency can be better served by an approach to localism that emphasizes not the autonomy of the local, but rather the capacity of localities to *initiate* and *innovate* policies.

Moral judgment and democratic mobilization

Democratic political agency requires not only the institutional spaces in which to act and the access to participate in those spaces; it also requires

substantive moral stakes that can animate and mobilize democratic political action. In democratic economic governance, the substance of economic policy should be understood not in technical or economistic terms, but as fundamentally moral and political judgments about what kind of economy we as a society hope to create.

As suggested in Chapter 5 above, the problem with technocratic governance is two-fold: not only does it tend to exclude citizens from the political power, but it also works to *sterilize* and *depoliticize* matters of substantive moral concerns, supplanting moral disagreements with technical ones that are amenable to resolution through recourse to expertise. Similarly, laissez-faire approaches shift economic concerns out of the domain of politics to the diffused ordering of the market, while converting these moral questions into a register prioritizing efficiency, growth, and market returns. But moral values are irrevocably embedded in complex policy disputes, particularly on such central issues as economic regulation. Just as a more democratic political economy requires a greater balance between citizen and expert in the policymaking process, it also requires a shift away from the aspiration to neutral technocratic discourse of policy, to a more openly moral debate that incorporates rather than being displaced by technical considerations.

As an example of this point, consider another famous Brandies dissent. In *New State Ice Co. v. Liebmann*,[55] Brandeis argued in dissent that the Supreme Court should have upheld Oklahoma's effort to confer a state-sponsored monopoly for the production of ice. This dissent is notable because in it, Brandeis articulated a distinctly Progressive view of economic policies as fundamentally

[55] *New State Ice Co. v. Liebmann*, 285 U.S. 263 (1934) (J. Brandeis, dissenting).

political and *moral* concerns. According to Brandeis, when companies provided necessities of life, these companies could be regulated more stringently as public utilities to ensure that the production and distribution of these goods were managed in accordance with the public good. Ice qualified as a necessity, and though private individuals were capable of manufacturing their own ice, the structure of production lent itself to a monopoly.[56] This view represents a very different understanding of public goods and the purposes of economic regulation that the kind employed today by the technocratic view of economic governance. Public goods in contemporary understandings are defined in economic terms, as goods whose production involves high sunk costs, increasing returns to scale, and are nonrival and nonexcludable. By contrast, Brandeis views public goods simply as those goods whose social value and importance justifies more robust political oversight. The role of regulation, then, is not purely economic; it is *political*, a way to ensure that we the people have a voice in shaping our economic order to achieve moral goals of economic justice.

Indeed, Brandeis argued that the "business of supplying to others, for compensation, any article or service whatsoever may become a matter of public concern," depending upon "the conditions existing in the community affected."[57] The public interest overrode any claims to insulation from state interference: "if it is a matter of public concern, it may be regulated, whatever the business."[58] Brandeis argued that "so far as concerns the power to regulate, there is no

[56] *New State Ice,* 285 U.S., 287-95.

[57] *New State Ice,* 285 U.S., 301.

[58] *New State Ice*, 285 U.S., 301.

difference, in essence, between a business called private and one called a public utility or said to be 'affected with a public interest.'"[59] As the power and importance of an industry increased, so too did the moral demands that this industry be subject to democratic accountability. Only the democratic public could determine which utilities or necessities were important enough and sufficiently concentrated in private ownership to warrant such aggressive public regulation. In contrast to contemporary views of private markets as inviolate, or of state regulation as limited to closing market failures, this Brandeissian account contemplates a more aggressive role for the state in regulating necessities through the exercise of political authority.

Economic policies are thus not purely a matter of 'private' market order, nor technical or economistic expert regulation, for they implicate moral and political concerns. Repoliticizing our understanding of economic policy has two important agency-enhancing effects. First, it opens these morally-weighty issues to greater democratic contestation by making the issues at stake more accessible to citizens, drawing them into political debate. Second, it facilitates a more nuanced and appropriate form of political judgment: if economic policies are inextricably moral as well as technical, ignoring the moral dimensions and delegating these policies purely to expert or market orderings submerges those moral judgments, resulting in pathological and problematic outcomes.

Engaging the moral dimensions of economic policies draws a wider array of citizen voices into these policy debates, thus broadening democratic agency. For citizen mobilization to be worthwhile in the first place, the issues at stake must be

[59] *New State Ice,* 285 U.S., 302.

understood as political in the sense that they are actionable through political mobilization.[60] As political scientist Deborah Stone explains,

> Difficult conditions become problems only when people come to see them as amenable to human action. Until then, difficulties remain embedded in the realm of nature, accident, and fate—a realm where there is no choice about what happens to us. The conversion of difficulties into problems is said to be the *sine qua non* of political rebellion, legal disputes, interest-group mobilization, and of moving policy problems onto the public agenda.[61]

The mobilizing effects of such moral discourses is particularly important for complex social problems that are, absent such a mobilizing narrative, difficult for isolated individuals to understand or make sense of. In these settings, it is only through the articulation of narratives and symbols that citizens can create new meanings and joint political action.[62] By tapping the concerns and passions of individual citizens and social groups, narratives draw them into the political arena.[63] By drawing people into a political debate, rhetoric and narrative can open up a more genuine space for political action.[64]

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[60] Mika LaVaque-Manty, A*rguments With Fists: Political Agency and Justification in Liberal Theory* (New York: Routledge, 2002), 18; Jeff Stout, *Blessed Are the Organized* (Princeton University Press, 2010), 160.

[61] Deborah Stone, "Causal Stories and the Formation of Policy Agendas" *Political Science Quarterly*, 104:2 (1989), 281-300, at 281.

[62] Dewey, *Public and Its Problems*, 153. See e.g., Margaret Somers, Fred Block, "From Poverty to Perversity: Ideas, Markets, and Institutions over 200 Years of Welfare Debate," *American Sociological Review* 70:2 (2005), 260-287; Stone, "Causal Stories"; Daniel Carpenter and Gisela Sin, "Policy Tragedy and the Emergence of Regulation: The Food, Drug, and Cosmetic Act of 1938," *Studies in American Political Development* 21 (Fall 2007), 149-180.

[63] See Hannah Pitkin, "Justice: On Relating Private and Public," *Political Theory* 9:3 (1981), 327-352. See also Seyla Benhabib, "Models of Public Space: Hannah Arendt, the Liberal Tradition, and Jurgen Habermas," in Craig Calhoun, ed., *Habermas and the Public Sphere* (Cambridge: MIT Press, 1996), 81-88, at 73-98; and Dana Villa, *Public Freedom* (Princeton: Princeton University Press, 2008), 207.

[64] See Brian Garsten, *Saving Persuasion: A Defense of Rhetoric and Judgment* (Cambridge: Harvard University Press, 2006), 13-19.

This moral mobilization also allows for a more appropriate form of political judgment. While it is tempting to delegate economic policies to neutral experts or markets, such a transference does not avoid moral controversy; it submerges it, moves it beyond the scope of citizens to contest. A more openly political language of policymaking helps counter the resultant subterranean value-judgments, opening them up to more broad-based scrutiny and contest.[65]

This view of democratic discourse and judgment thus provides a way to engage in meaningful democratic empowerment of citizens without necessarily appealing to heroic civic virtue of citizens as dispassionate public reasoners, but neither does this approach imply an adoption or resignation towards the relatively limited capacities of current democratic citizens.[66] Despite anxieties of manipulation, pandering, or explosive conflict, moralized political discourse is crucial for engaging our individual and collective capacities for judgment, where decisions are reached not through technical rationality or consensus, but through persuasion, and provisional decisions that can be revisited in the future.[67] Non-deliberative conflict, bargaining, and debate can be a complement to deliberation,

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[65] Note that this is a very different approach from most critiques of "backroom politics"—the problem here is not the contamination of neutral regulatory policymaking by political influence; rather it is the submerging of politics behind a language of technocratic policy science thereby undermining the ability of less well-connected groups to challenge and contest the policy in question.

[66] For a recent defense of the citizen-as-spectator, see Jeffrey Green, *The Eyes of the People: Democracy in an Age of Spectatorship* (New York: Oxford University Press, 2010). Green rightly highlights the degree to which "candor" is a central enabler of popular power, linked to but distinct from familiar democratic theory concepts of deliberation, participation, and transparency. But unlike Green, I see this as simply one element of democratic political agency—and as an element that helps empower citizens to be more than spectators.

[67] See Garsten, *Saving Persuasion*, 174.

for example by forcing an actual decision, or by creating a background set of commitments and threats that facilitate genuine deliberation between parties.[68]

This appeal to the "ideal of rhetorical deliberation" is vital for protecting and expanding the scope for democratic politics itself: "In a time when we find our lives increasingly governed by the standardized rules of large bureaucracies and corporations and by the technocratic decisions of policy-making experts, it is important not to lose track of our natural human capacity to make sense of complex situations for ourselves," rather than alienating our judgment as citizens to other political actors supposedly better situated to achieve understanding and agreement.[69] Such an abandonment of political passion undermines the scope for democratic agency, reducing citizens and actual victims of injustice to "passive roles, as objects of pity and as potential beneficiaries of properly rationalized decision making."[70] In turn, this exclusion of an active role for citizens is likely to magnify the very pathologies of democratic discourse that we rightly fear. By distancing citizens from the project of governance and political judgment removes them from the practice of argument and decision-making, as well as from the outcomes of those decisions. This distance ironically creates a greater scope for dogmatic forms of rhetoric and unfocused or irresponsible forms of political discourse, even as it narrows the scope for meaningful political engagement.[71]

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[68] See e.g. Jane Mansbridge, with James Bohman, Simone Chambers, David Estlund, Andreas Follesdal, Archon Fung, Cristina Lafont, Bernard Manin, and Jose Luis Marti, "The Place of Self-Interest and the Role of Power in Deliberative Democracy," *Journal of Political Philosophy* 18:1 (2010), 64-100.

[69] Garsten, *Saving Persuasion*, 175.

[70] Stout, *Blessed Are the Organized*, 65.

[71] See Garsten, *Saving Persuasion*, 175.

Democracy as a response to economic crisis

Where the tradition of technocratic economic governance as manifested in the New Deal and Obama era economic policy responds to economic upheaval through an appeal to neutral, centralized expertise, a different normative tradition turns instead to the potential of empowered democratic citizens. This tradition has roots in the radical democratic thought of the Progressive Era, and carries important implications for today.

Indeed, Brandeis explicitly tied his call for democratic agency through local governments and public utilities as an imperatives of the Great Depression itself. Brandeis closes his *New State Ice* dissent with a clarion call for democracy as a response to the economic crisis. "The people of the United States are now confronted with an emergency more serious than war," Brandeis intoned.[72]

> Misery is widespread, in a time, not of scarcity, but of overabundance. The long-continued depression has brought unprecedented unemployment, a catastrophic fall in commodity prices, and a volume of economic losses which threatens our financial institutions. Some people believe that the existing conditions threaten even the stability of the capitalistic system. Economists are searching for the causes of this disorder and are re-examining the basis of our industrial structure. Business men are seeking possible remedies.

While the Depression drove many commentators to call for "some form of economic control," how exactly a democratic society could effectively manage the tempests of the modern economy remained unknown. "The economic and social sciences are largely uncharted seas," and current policymakers "have been none too successful in the modest essays in economic control already entered upon."

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[72] *New State Ice*, 285 U.S., 310-11.

The formulation of perfect policies in such complex settings would require "some measure of prophecy," given that "man is weak and his judgment is at best fallible." As a result, Brandeis argued, there was no choice but to allow for social learning through the actual experience of policy innovation, development, and experimentation:

> There must be power in the states and the nation to remould, through experimentation, our economic practices and institutions to meet changing social and economic needs. I cannot believe that the framers of the Fourteenth Amendment, or the states which ratified it, intended to deprive us of the power to correct the evils of technological unemployment and excess productive capacity which have attended progress in the useful arts. … To stay experimentation in things social and economic is a grave responsibility. Denial of the right to experiment may be fraught with serious consequences to the nation. It is one of the happy incidents of the federal system that a single courageous state may, if its citizens choose, serve as a laboratory; and try novel social and economic experiments without risk to the rest of the country.

Similarly, Dewey saw the economic upheaval of the new industrial economy as a fundamental threat to liberty that had to be met through a renewal of democratic institutions. Liberty, for Dewey, meant "effective power to do specific things."[73] Promoting human freedom meant expanding the capacities of individuals to achieve self-realization.[74] Freedom as experienced in the world was necessarily relational and constituted by social arrangements: "the liberties that any individual actually has depends upon the distribution of powers or liberties that exists, and this distribution is identical with actual social arrangements, legal and political–and, at the present time, economic."[75] The task of promoting

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[73] John Dewey, "Liberty and Social Control," (1935), in *Later Works of John Dewey, 1925-1953, vol. 11: 1935-1937*, 359-363, at 359.

[74] John Dewey, *Liberalism and Social Action* (New York: Prometheus, 2000), 34.

[75] Dewey, "Liberty and Social Control," 362.

human freedom would therefore require reforms to existing economic arrangements–and the creation of genuinely democratic modes of economic governance:

> Effective liberty is a function of the social conditions existing at any time…as economic relations became dominantly controlling forces in setting the pattern of human relations, the necessity of liberty for individuals which they proclaimed will require social control of economic forces in the interest of the great mass of individuals.[76]

The very socioeconomic upheavals that created the urgency for greater economic regulation driven by democratic action also created "new conditions" that would enable "the release of human potentialities previously dormant."[77] By tapping greater possibilities of social welfare and democratic empowerment, Progressives could realize genuine human emancipation and freedom.[78]

To achieve such self-rule, however, required new institutional structures. Dewey argued there was "no sanctity" to particular received "devices" of democratic elections.[79] Instead, institutions could take a variety of forms so long as they ensured that a "scattered, mobile and manifold public may so recognize itself as to define and express its interests."[80] As Dewey wrote,

> The old saying that the cure for the ills of democracy is more democracy is not apt if it means that the evils may be remedied by introducing more machinery of the same kind as that which already exists, or by refining and perfecting that machinery. But the phrase may also indicate the need of returning to the idea itself, of clarifying and deepening our apprehension of

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[76] Dewey, *Liberalism and Social Action*, 43.

[77] Dewey, *Public and its Problems*, 98.

[78] Dewey, *Public and its Problems*, 99-100.

[79] Dewey, *Public and Its Problems*, 145.

[80] Dewey, *Public and Its Problems*, 146.

> it, and of employing our sense of its meaning to criticize and re-make its political manifestations.[81]

Neither Dewey nor Brandeis offered a systematic theory of democratic agency, but their ideas—informed crucially by their own experiences as activists and reformers—point us towards three key conditions for democratic political agency in context of economic reform debates: participatory access, institutional forums, and moralized terms of debate.

These three conditions combine and reinforce one another to provide citizens with meaningful political agency as co-authors of economic policy, operating alongside experts without being supplanted by them. Moral discourses help catalyze and mobilize citizen action, opening economic policy issues to a broader normative debate. To engage this debate, citizens must have political power to shape policies alongside experts. But to channel these citizen energies effectively, there must be institutions that can act as forums, targets, and spaces for democratic judgment.

This democratic approach to economic governance suggests a very different alternative to either the reliance on markets in laissez-faire thought, or the turn to neutral expert management in technocratic thought. The technocratic view of economic governance responds to the challenges posed by the market economy by appeals to neutral purposes of market optimization, and by relying on the idyll of neutral experts pursuing an objectively verifiable public good. By contrast, this democratic economic governance view takes a different approach. Institutions of regulatory governance become a way to respond to the threats of the market

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[81] Dewey, *Public and Its Problems*, 144.

economy by magnifying, fostering, and catalyzing the democratic agency of citizens themselves.

The final three chapters show how these themes might inform concrete policy and institutional debates in financial regulation and public law of democratic institutions more generally.

Chapter 8 examines the structure of the modern regulatory state to outline how it might be reformed to provide a more consolidated target and forum for democratic action, with a more participatory role for citizens, and a more openly normative discourse of policymaking. Regulatory agencies already possess broad powers, but they lack these other democratizing conditions described above. As spaces for democratic action, cities, by contrast, have the inverse problem: they offer more opportunities for participation and political judgment, but they lack expansive political authority, thus undermining their value as democratic forums. Chapter 9 therefore examines this problem of city power, as a way of recovering the democratic potential of cities as a second front-line institution for democratic economic governance.

Chapter 10 examines the importance of moralized judgment over economic policy matters, showing how the technocratic impulse to depoliticize these economic policy issues limits our menu of reform alternatives by taking more moralized policy options off the table. This chapter also argues that this effort to depoliticize economic policy drives us to build technocratic institutions for economic governance that cut against the democratizing approaches argued for above, by centralizing authority in expert-led institutions divorced from moral and political judgment. But in our attempt to sidestep moral controversy, we instead displace it into a set of proxy debates over the reach of regulatory authority. These

proxy debates in turn create their own pathologies that paradoxically worsen, rather than resolve, the kinds of moral concerns raised by the modern economy.

PART III

8 DEMOCRACY THROUGH REGULATION

Economic policy is not just a technical matter to be delegated to expert-led regulatory institutions. These issues concern fundamental moral and political judgments. But addressing these moral dimensions also requires an institutional context conducive to democratic contestation by citizens. As discussed in Part II, regulatory institutions can facilitate democratic empowerment by providing participatory access for citizens to policymaking decision; providing a clear focal point for citizen action; and by engaging with moral and political concerns and debates. This chapter develops each of these themes to highlight some avenues through which national regulatory agencies can be reconstructed as more democratic, rather than technocratic, forums.

Participation and representation within agencies

While the phrases "public participation" and "public involvement" appear codified hundreds of times in the US Code and thousands of times in the Code of Federal Regulations as requirements for regulatory agencies, these terms are not formally defined, and rarely come with specific requirements or processes.[1] Indeed, on paper, the regulatory state includes a variety of channels for citizen participation, including requirements for public notice-and-comment, and ad hoc

[1] Lisa Bingham, "The Next Generation of Administrative Law: Building the Legal Infrastructure for Collaborative Governance," *Wisconsin Law Review* 2010, 297-357, at 317-23.

stakeholder forums convened by agencies. But these mechanisms do not provide meaningful political power for citizen groups. Notice-and-comment, for example, is used by agencies selectively as a source of information, data, or justification for already-determined policies, while sophisticated interest groups are most successful and influencing agency rulemakings.[2] To make regulation a more genuinely democratic process, citizens must be able to participate in more meaningful ways, as co-authors of regulatory policies. There are two possible vectors for such empowered participation in regulation. First, regulatory agencies can incorporate greater forms of interest representation, facilitating the mobilization and voice of stakeholder groups within regulatory policymaking. Second, agencies can engage citizen participation in a more ongoing fashion, in the implementation and revision of policies themselves.

Representation in regulation

During the 1960s and 1970s, judicial doctrine attempted to promote interest representation and greater citizen participation in regulation, but these measures were extremely controversial and quickly abandoned. From a democratic perspective, the failure of this interest representation approach is not surprising; simply opening the regulatory process to interest group pluralism as attempted with limited results earlier does not solve the challenges of facilitating collective action by diffuse and under-resourced groups.[3] Empirical studies suggest that while

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[2] See e.g. Mariano-Florentino Cuellar, "Rethinking Regulatory Democracy," 57 *Administrative Law Review* 411 (2005).

[3] Steven Croley, *Regulation and the Public Interests: The Possibility of Good Regulatory Government* (Princeton: Princeton University Press, 2008), 54-55.

influence may be more balanced then resources of different groups, business interests generally participate more, and groups that can offer more sophisticated input through comment procedures—particularly more resourced groups—tend to have greater influence.[4]

To address these difficulties, a revamped administrative process that structures stakeholder representation and citizen engagement can facilitate more balanced contestation of regulatory policies.[5] Instead of passively relying on interest groups to mobilize and lobby agencies, regulatory institutions must proactively engage and consult all affected interests. Furthermore, these consultations with stakeholders must have real policy stakes and repercussions, rather than simply providing input to regulators. Stakeholder engagement requires institutions that build in contestation, diversity of views, and empower the countervailing power of citizen and public interest groups.[6]

This kind of more empowered consultation can be achieved by taking advantage of untapped opportunities in the regulatory state for more meaningful representation of stakeholders. Indeed, existing mechanisms to consult stakeholders in regulatory policymaking have been understood *not* as channels for democratic representation and deliberation, but rather as an epistemic task of securing more expert information and input for technocratic regulation.[7] The

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[4] See Croley, *Regulation and the Public Interests*, 125-33, Cuellar, "Rethinking Regulatory Democracy".

[5] Croley, *Regulation and the Public Interests*, 134-41.

[6] Christie Ford, "New Governance in the Teeth of Human Frailty: Lessons from Financial Regulation," *Wisconsin Law Review* 2010, 441-489, at 485-86.

[7] Mark Brown, *Science in Democracy: Expertise, Institutions, and Representation* (Cambridge: MIT Press, 2009), 242.

General Services Administration guidelines for agencies employing advisory committees under the Federal Advisory Committee Act (FACA) describe FACA as "not a participation statute," though it is a "means of obtaining public involvement."[8] But when initially proposed, the issue of whether FACA was meant to facilitate stakeholder representation or input for technocratic regulation was hotly contested.[9] The early drafts of FACA in the House called for committees to be "fairly balanced in terms of points of view represented," and included a specific list of stakeholders to be granted representation, such as conservation, environmental, consumer, and public interest groups.[10] The Senate versions of the bill, however, avoided specific the representational requirements of the House version.[11] The final compromise bill took a more middle path requiring that advisory committee membership "shall be representative of those who have a direct interest in the purpose of such committee."[12] While the conference committee report adopted the more representational formulation of HR 4383, subsequent judicial rulings used the Senate language to interpret the representation requirements along the more permissive lines envisioned by the Senate.[13] The use

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[8] 41 CFR parts 101-6, 102-3, FR 37728-37750 (2001), cited in Brown, *Science in Democracy*, 243.

[9] Sheila Jasanoff, *The Fifth Branch: Science Advisors as Policymakers* (Cambridge: Harvard University Press, 1990), 36-7.

[10] HR 4383 (1970), cited in Brown, *Science in Democracy*, 94-103.

[11] See S. 1637 (requiring at least one third of members to be "knowledgeable and competent to represent the interests of the public); S. 1964 (with a more vague requirement of fairly balanced advisory committees); S. 2064 (requiring committees be "representative of all those legitimately interested" in the committee functions; cited in Brown, *Science in Democracy*, 94-103.

[12] S. 3529, in Brown, *Science in Democracy*.

[13] *National Anti-Hunger Coalition v Executive Committee of the President's Sector Survey on Cost Control* (557 F Supp 524, DDC 1983); *Public Citizen v National Advisory Committee on Microbiological Criteria for Foods*, 886 F. 2d 419, DC Cir 1989), cited in Brown, *Science in Democracy*.

of FACA thus generally presumes that experts on the commission do not have specific interests, while representatives of interests do not have expertise.[14] Instead, the role and power of these committees could be altered to play a more direct role in shaping regulatory policy, with a charge to ensure balanced representation of all affected interests.

Dodd-Frank itself took some tentative steps towards greater stakeholder representation in financial regulation. Many of the industry-friendly financial regulations like the SEC's capital adequacy rules—which were relaxed in the run-up to the 2008 crash—were developed through what on paper appeared as a consultative process engaging with industry stakeholders. Yet the lack of an institutionalized representation or countervailing voice from public interest groups and other citizen organizations removed a vital check that could prevent such consultations from being overly favorable of and solicitous to industry interests.[15] Although its primary focus is on the expansion of expert regulatory oversight, the Dodd-Frank financial reform bill included some provisions aimed at promoting a more balanced representation of interests in financial regulation. One example of this approach is the Dodd-Frank Act's creation of an Investor Advisory Committee, which is tasked with advising the Financial Stability Oversight Council (FSOC) on regulatory reforms to protect investors.[16] The Committee is comprised of a mix of representatives of various stakeholder interests, such as state

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[14] Brown, *Science in Democracy*, 103.

[15] See e.g. Robert Weber, "New Governance, Financial Regulation, and Challenges to Legitimacy: The Example of the Internal Models Approach to Capital Adequacy Regulation," *Administrative Law Review* 62 (2010), 783-870.

[16] Dodd-Frank Act § 901-911 (to be codified at 15 U.S.C. § 78).

governments, senior citizens, and pension funds, in addition to relevant experts.[17] Further, the Committee includes an Investor Advocate, who is explicitly empowered to head an advocacy unit within the network of financial regulatory agencies.[18] The office of the Investor Advocate lobbies the SEC to promote policies favorable to investor interests,[19] and also provides a forum for individual investors to lodge complaints and report lapses in compliance with financial regulations.[20] Other provisions in the pieces of legislation attempt to achieve balanced representation of interests by requiring stakeholder membership on rulemaking or advisory boards. For example, the financial reform act includes a provision to establish a Municipal Securities Rulemaking Board, comprised of experts and representatives of brokers, investors, and the general public, to set standards for municipal securities advisors.[21]

Participation in implementation and revision

Such participation and engagement of citizens should also extend not only to the initial formulations of agency policies, but also to the implementation, monitoring, and revision of policies as they are put into practice. This more expansive view of participation would provide citizens with a more meaningful experience of governance, involving them in multiple stages of the policy process.

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[17] *Ibid*.

[18] *Ibid*.

[19] Dodd-Frank Act § 915 (to be codified at 15 U.S.C. § 80b-11 note).

[20] Dodd-Frank Act § 919D (to be codified at 15 U.S.C. § 78d).

[21] Dodd-Frank Act § 973-976 (to be codified at 15 U.S.C. § 78).

For example, the National Environmental Policy Act (NEPA) provided avenues for community groups to participate in and put pressure on the permitting process for licensing the sites of potentially hazardous industrial activities.[22] Revision of regulations also would benefit from participatory review.[23] Indeed, many agencies already employ some form of retroactive review of existing regulations, sometimes mandated by statute, but more often the result of a more ad hoc, informal intra-agency policy process. These reviews are, as a result, of minimal impact, often lacking support from agency management, with limited public engagement, and unclear standards or best practices.[24]

In context of financial regulation, the most compelling example of this kind of participatory democratic engagement is the role of community groups in enforcing the Community Reinvestment Act. The Community Reinvestment Act (CRA) of 1977 encourages federally insured banks and thrifts to meet local community credit needs.[25] Federal agencies examine these financial institutions to rank their CRA performance.[26] These rankings, in addition to public comments on

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[22] See e.g. Luke Cole, "Macho Law Brains, Public Citizens, and Grassroots Activists: Three Models of Environmental Advocacy," *Virginia Environmental Law Journal* 14 (1994) 687-710 (arguing for the need to build on the access granted by the NEPA permitting procedures by mobilizing local citizens into community groups capable of influencing firms and regulatory overseers).

[23] See e.g. *FCC v. WNCN Listeners Guild*, 450 U.S. 582 (1981), Marshall dissenting for a similar argument (arguing that complex agency policies should include a formal 'safety valve' procedure allowing affected and public interest groups to raise concerns about the policy as it is implemented and as social conditions change).

[24] GAO, "Reexamining Regulations: Opportunities Exist to Improve Effectiveness and Transparency of Retrospective Reviews," Report to Congressional Requesters, July 2007 (GAO-07-791).

[25] See 12 USC 2901-8 and 1831u(b)(3) (CRA provision for interstate mergers) and 1843(l)(1)-(2)(CRA requirement for financial companies to expand financial activities); see also Michael Barr, "Credit Where It Counts: The Community Reinvestment Act and Its Critics," *NYU Law Review* 74 (2005), 100-233, at 104-5.

[26] Different agencies are responsible for overseeing different kinds of financial institutions. The CRA applies to each of these agencies as they oversee their relevant financial institutions. Thus, the

the CRA activities of these firms, are considered when financial regulatory agencies examine merger applications and requests by these firms for opening and closing new branches. Further, individuals and community groups can request to review a firm's CRA records, comment on it CRA activities, and file challenges when these firms apply for regulatory approval of the CRA contingent transactions such as mergers. Where agencies find banks to have insufficiently met their CRA obligations, these community groups can propose alternative lending practices and projects, leading to a negotiation between the firm, the community, and the regulatory agency.[27] This regulatory oversight became more effective after 1995 regulations and revisions which specified three tests by which these firms would be evaluated: a lending test, and investment test, and the service test.[28]

The evidence suggests that banks have, as a result of the CRA, changed their behavior, forming multibank Community Development Corporations, investing in locally based Community Development Financial Institutions, and dedicating special units to focus on meeting the needs of local low and moderate income borrowers within the geographic area of the bank orders or branch.[29] Ultimately, the CRA has proven to be an effective response to discrimination in mortgage lending and capital flight, driving the expansion of low income and

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OCC oversees national banks, the Federal Reserve oversees state-chartered banks that are members of the Federal Reserve system, the FDIC oversees state-chartered banks that are not members of the Federal Reserve system. See Richard Marisco, "Democratizing Capital: The History, Law, and Reform of the Community Reinvestment Act," *New York Law School Law Review* 49 (2004), 712-726, at 718.

[27] Raymond Brescia, "Part of the Disease or Part of the Cure: The Financial Crisis and the Community Reinvestment Act," *South Carolina Law Review* 60 (2008), 618-677, at 635-6.

[28] Barr, "Credit Where it Counts," 112.

[29] Barr, "Credit Where it Counts," 147-48.

minority borrowing and locally rooted community investment— while maintaining sound lending practices and bank profitability.[30]

But the real unique strength of the CRA framework lies in its harnessing of democratic participation as part of its enforcement regime. The CRA bolsters local community involvement both by incentivizing banks to lend to local businesses, and empowering community-based organizations as local brokers who can match worthy borrowers with willing banks.[31] This mobilization is what made the CRA effective in changing bank behavior. In a number of cities, the CRA's provision allowing community groups to invoke federal regulatory involvement helped catalyze a broader effort among community organizations to organize and expand their engagement with local banks.[32] The background threat of federal regulatory enforcement incentivized banks themselves to engage with these community groups and negotiate for mutually agreeable community lending programs.

For example, in Boston in the 1990s, groups like the Community Investment Coalition formed out of a combination of labor unions, community development corporations, and the state Affordable Housing Association. The CIC then developed neighborhood reinvestment plans for the Roxbury area of Boston, and prepared CRA challenges. In response, many of the larger banks of the area including the Bank of Boston and that Bank of New England agreed to negotiate, culminating in an affordable mortgage lending plan for the region.[33]

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[30] See Barr, "Credit Where it Counts"; and Brescia, "Part of the Disease or Part of the Cure."

[31] Barr, "Credit Where it Counts", 128.

[32] Gregory Squires, "Rough Road to Reinvestment," in Gregory Squires, ed., *Organizing Access to Capital*, (Temple University Press: Philadelphia, 2003), 1-26.

[33] William Tisdale and Carla Westheirn, "Giving Back to the Future: Citizen Involvement and Community Stabilization in Milwaukee," in Squires, ed., *Organizing Access to Capital*, 42-54.

Similarly, in Pittsburgh, the Community Reinvestment Group formed a multiracial advocacy coalition in 1988 to conduct research on CRA scorecard data provided by federal agencies. Invoking the CRA, this group was able to organize and empower other community development corporation leaders, and negotiate with local banks to channel more investment to poorer neighborhoods. The group even convinced the city of Pittsburgh and the Board of Education to put its money in banks that performed better on their CRA obligations.[34]

The participation and engagement of these community groups exemplifies an important way in which democracy can facilitate the implementation and enforcement of regulatory policies. First, citizen participation can help identify practices which contravene the goals of the regulation, by harnessing defused grassroots networks of observers and participants who collectively have greater monitoring capacity than any centralized agency. Second, the presence of organized community groups can help better balance of viewpoints represented during the implementation of regulations. Such empowerment of community groups can provide a counterweight to hold both regulated firms and federal agencies accountable for their actions—or, more likely, their inactions. In the absence of active community groups mobilizing to pressure local banks, it seems likely that these banks' CRA failures would have gone unnoticed, or ignored by the agency. Even if failures were noted, without the vocal engagement of community groups, it would be easier for banks to nominally discharge their CRA obligations without necessarily needing the actual needs of the local community. Third, by fostering ongoing participation and engagement, the CRA approach can help drive

[34] Stanley Lowe and John Metzger, "A Citywide Strategy: The Pittsburgh Community Reinvestment Group," in Squires, ed., *Organizing Access to Capital*, 85-101.

the emergence of social norms about the local economy and greater civic education and sophistication over time. Citizen participation of this form thus offers epistemic benefits for implementing regulations; political benefits by shifting the balance of power in a way that gives more effective voice to community groups that might otherwise be silent; and normative benefits of fostering norms and civic engagement.

Today, the CRA has less of an effect on bank lending or on community participation. CRA oversight is now more generally a process of agency rubberstamp approval, while courts have been hostile to legal challenges from individuals and groups seeking judicial review of agency decisions under the CRA.[35] These trends have diminished the ability of community groups to monitor bank and agency conduct. However, as a model, the CRA experience is instructive. By establishing a mutually reinforcing interaction between regulatory agencies and local citizen and community groups, the CRA suggests ways in which citizen participation can be harnessed to improve the enforcement and implementation of regulations, and to help check the actions of both industry groups and agencies themselves. Further, such democratic engagement helps foster a broader public discourse about social norms, values, and civic empowerment. Indeed, the CRA approach of fostering participation is arguably more effective than other regulatory approaches such as disclosure, product regulation, or legal enforcement of antidiscrimination laws, in large part because of the of the ways in which

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[35] Brescia, "Part of the Disease or Part of the Cure," 652-5. See e.g. *Lee v. Board of Governors of the Federal Reserve System*, 118 F.3d 905 (2d Cir 1997) and *Lee v. Federal Deposit Insurance Corporation*, SDNY 1997, discussed in Brescia, 655-61.

participation enables broader more effective monitoring of compliance, and fosters longer-term generation of social norms and civic empowerment.[36]

This virtuous dynamic of democratic engagement and effective regulatory enforcement derives from a particular institutional configuration of the CRA enforcement approach. Several conditions in particular stand out. First, there are clear metrics with which to evaluate banks CRA performance, provided publicly by federal agencies.[37] Second, community groups are empowered to request examinations or hearings focusing on the CRA activities of local banks. Third, the conditioning of merger approval on a good CRA scorecard in context of a period of intensified merger activity gave the CRA review process actual bite, thus creating a strong incentive for banks to engage with community groups and agencies to achieve a better CRA score.[38] Fourth, the CRA evaluations conducted by agencies and the public hearings requested by community groups are all public, with multiple groups involved, making rent-seeking hard to conceal.[39] Indeed, only a fraction of a percent of community investment funds arising from CRA negotiations went to the community organizations themselves, suggesting very little rent seeking.[40] Finally, the CRA specifies a standard of the meeting the needs of the local community, rather than specifying a rule for what this might mean. Not only does this standards-based approach offer a more flexible and adaptable framework, it also helped generate citizen participation in interpreting what local

[36] See Barr, "Credit Where it Counts," 210-29.

[37] Barr, "Credit Where it Counts," 113.

[38] Barr, "Credit Where it Counts," 113.

[39] Barr, "Credit Where it Counts," 173.

[40] Barr, "Credit Where it Counts," 174.

needs might be, and evaluating whether those needs have been met. This standards-based approach thus enabled a more democratically-driven form of norm creation as local citizens participated in defining what their needs were and monitoring compliance against those needs.[41]

Empowering citizens in regulation

Such expanded and empowered participation can be facilitated by the political branches. Explicit statutory schemes enabling participation and standing can overcome the ambiguities of legal doctrine and provide a more robust institutional structure for participation. Similarly, executive orders could establish baseline procedures that systematize and thicken ad hoc agency practices of citizen participation, stakeholder consultation, and retrospective reviews. Such executive orders could also provide defined standards and criteria for participation.[42] It is telling that under the current Executive Order 12866, the regulatory review process run by the Office of Management and Budget (OMB) focuses almost entirely on the cost-benefit analysis and regulatory impact analysis prepared by agencies, with little attention paid to *who* the agency consulted, and how. Further, OMB and its sub-agency the Office of Information and Regulatory Affairs (OIRA) are required under EO 12866 to accept requests from individuals and groups seeking meetings to voice their concerns about a particular regulation, but these meetings are one-way sessions, not open deliberations. In part this narrow

[41] Barr, "Credit Where it Counts," 183-6.

[42] Bingham, "The Next Generation of Administrative Law," 350-6 (proposing language for a new executive order).

structure is meant to allow some form of voice without further plunging the regulatory review process in political debate, on the assumption that such deeper debate took place at the agency level. But a better structure for regulatory review might require more of agencies at the initial policymaking stage in terms of participatory engagement and consultations, while tasking OIRA with reviewing not just the technocratic policy analysis, but also whether agencies have adequately complied with such participatory requirements. More generally, participation can be fostered through the formation of a regulatory agency that is itself specialized in structuring participatory processes, and dedicated to establishing overall goals, processes, training, incentives, and measures of success for enabling participation.[43]

Meanwhile, administrative law can play a role in helping realize this approach of participatory regulation. First, legal doctrine and judicial review should be changed to expand judicial protections for citizen participation in regulatory policymaking. In the late 1960s and early 1970s, legal doctrine provided greater support for citizen participation in agency policymaking.[44] Second, legal doctrine can broaden standing requirements enabling citizens and associations to challenge agency actions in courts—particularly by enabling citizen suits to challenge violations of procedural harms in the regulatory process. Doctrine has often backed away from broad readings of standing with respect to administrative agencies, casting a shadow over the ability of citizens and groups to challenge agency actions even when these actions seem to violate some procedural

[43] Charles Sabel and William Simon, "Minimalism and Experimentalism in the Administrative State" (unpublished manuscript, on file with author, 2011), at 27-30; Cuellar, "Rethinking Regulatory Democracy," 491-97.

[44] See generally, Richard B. Stewart, "The Reformation of American Administrative Law," *Harvard Law Review* 88:8 (June 1975), 1669-1813.

requirement or the interests seemingly promoted by Congressional statute.[45] Establishing a more firm right to challenge regulatory procedural harms in court, combined with greater statutory and agency policies to institutionalize consultative, representative, and participatory processes discussed above, would help consolidate the ability of citizens to engage directly in the business of regulatory policymaking.

Agencies as democratic forums

Suppose you are one of the many citizens who suffered as a result of the 2008-9 financial crisis and the subsequent economic downturn. You may have lost your job as one of the many newly-unemployed, or you may be a homeowner who is now underwater with a house worth less than the mortgage. You may have been victim to predatory lending, or you may have lost your pension. As a political actor, you may be motivated to support, advocate for, or help drive some policy response. In traditional democratic politics, your primary avenue to do so involves selecting a party or candidate to vote for, or to join a civil society advocacy organization. But before such participation or advocacy can take place, there is an even more fundamentally prior question: where would you even go to make your claims? This question is not so simple as it may seem at first. A visit to your local Congressperson's office may help, but the gap between your complaint as a constituent and a final resultant policy is vast, mediated not only by the

[45] See *Lujan v. Defenders of Wildlife*, 504 U.S. 555 (1992) (noting that "only a generally available grievance about government—claiming only harm to his and every citizen's interest in proper application of the Constitution and laws, and seeking relief that no more directly and tangibly benefits him than it does the public at large" does not have standing under Article III of the Constitution.)

legislative process, but perhaps more importantly, but the process of regulatory implementation. Your voice would be much more effective and meaningful if you could engage in some manner with the frontline institutions charged with the actual formulation and implementation of final policies—such as the actual regulatory agencies or local bodies that form the edges where the state meets the citizenry. But even here, the question of where to target your claims is murky at best. Among federal agencies, which of the many overlapping economic regulatory bodies would be the appropriate target for a complaint or proposal post-financial crisis? The Fed? The Securities and Exchange Commission? Or the Federal Housing Authority?

Regulatory agencies can help respond to this challenge to democratic political agency through two mechanisms. First, agencies can be constructed to provide visible focal points, readily identifiable targets for citizen mobilization and voice. But for agencies to provide a forum in this manner, we must rethink the way we approach the question of agency jurisdiction and specialization. In particular, we must balance between multiple specialized agencies on the one hand, and a more consolidated regulatory power on the other. Consolidation enables a forum to be more visible as a target and focal point for mobilization, while decentralization can facilitate access to the forum by multiplying potential sites of democratic engagement. Further, an overly fragmented administrative state conduces to turf wars and clashes that can cause different agencies to be more likely captured by different interests, while key issues fall between the cracks of regulatory authority or are deadlocked by clashes between agencies with overlapping jurisdictions. Thus, different agencies could be reorganized to have clearer authority over particular issues with clear links to particular social

interests.[46] Topical consolidation of agency authority can also facilitate accountability by improving the clarity of responsibility that voters and citizens can ascribe to particular agencies, while also enhancing the ability of particular agencies to act.[47]

Second, in addition to providing a visible target, agencies can act as dedicated representatives charged with acting on behalf of particular underrepresented or marginalized constituencies. Countervailing citizen interests can be represented through such "proxy advocacy," where a regulatory office is created with the explicit mission of representing the needs of a particular demographic of citizens—such as consumers, veterans, farmers—through advocacy, providing information to other regulators, and navigating the rulemakings process with an eye towards protecting these interests.[48] These regulatory offices would act not as neutral experts, but as representatives of a particular social interest, identifying and channeling its concerns within the broader ecology of regulatory agencies and the policymaking process. Such an agency could help underrepresented social groups participate in and put pressure on regulatory policy debates on par with more sophisticated insider interest groups.

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[46] See e.g. Keith Bradley, "The Design of Agency Interactions," *Columbia Law Review* 111:4 (May 2011), 745-94, at 778-83.

[47] See Jacob Gersen, "Unbundled Powers," *Virginia Law Review* 96 (2010), 301-360, at 309-15, 329-40.

[48] See e.g., Daniel Schwarcz, "Preventing Capture Through Consumer Empowerment Programs: Some Evidence from Insurance Regulation," in David Moss and Dan Carpenter, eds., *Preventing Capture* (Cambridge University Press, forthcoming, 2013) (examining case studies of how proxy advocacy and tripartism has helped mitigate the risk of capture in state-level insurance regulation).

These two mechanisms for agencies to facilitate democratic action—by offering a visible, consolidated authority for citizens to target, or by actively representing particular social interests—come to the fore in the financial reform context through the debate over the recently created Consumer Financial Protection Bureau (CFPB). As an institution charged with channeling and responding to consumer interests, the CFPB arguably attempts to overcome the existing fragmentation of the financial regulatory system by providing a consolidated forum and target for consumer finance policies. Indeed, one criticism of the pre-crash regulatory structure was that the proliferation of specialized financial regulatory agencies carved up the substantive issue of "financial sector regulation" in a way that tracked the specialization of regulatory agencies, but which made it increasingly difficult for non-bank interests to engage in the policymaking process and act as a countervailing force to the banking lobby. It also led to many key policy issues 'falling through the cracks'. The proposal to create a consolidated Consumer Financial Protection Bureau offers one way of re-slicing this same policy space—the CFPB centralizes authority in one agency, thus clarifying lines of accountability and responsibility, and providing a clear target against whom stakeholder groups can make claims.

At the same time, the tension between the agency as representative and the agency as neutral arbiter is particularly acute as the CFPB begins its work. The agency and its public discourse continues to conceive its role as an expert regulator in the mold of other regulatory agencies. Yet, many individuals working in the CFPB are themselves veterans of consumer rights advocacy bodies, and have close ties to the consumer rights movement. The CFPB in many ways embodies the same tension that lay at the heart of the persona of its progenitor, Elizabeth Warren: just

as Warren spoke the language of expertise but drew much of her popular support from her image as a zealous advocate for consumers, families, and those left behind in the financial crisis, so too does the CFPB speak the language of traditional expert regulation, while also serving as a foothold for consumer interests and a potential counterweight to the influence of otherwise sophisticated and well-connected banks and other lobbying groups. It is notable that the CFPB's grant of authority in Dodd-Frank includes the creation of subunits charged with protecting underserved communities and older Americans[49] and gives directives to ensure fair lending and equal access to credit.[50] The CFPB operates an office of community affairs office charged with organizing outreach to consumer advocacy groups and seeking input from constituencies like minorities, students with debt, and homeowners. Indeed, the realization that the CFPB may develop into a powerful advocate on behalf of consumers within the federal government likely animated much of the vociferous opposition to it on the part of banks and some conservatives.[51] It is notable that Dodd-Frank tempers the power of the CFPB in ways that very few other agencies are constrained. The statute requires the CFPB to consult and coordinate with the SEC, the CFTC, and the FTC.[52] Further, other

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[49] See Dodd-Frank Act § 1013.

[50] See Dodd-Frank Act § 1021.

[51] It is worth noting that several Republican legislative efforts sought to strip the CFPB of its independence in an effort to undermine its potential power. See, e.g., Shelby Amendment, S. Amdt. 3826, 111th Cong. (2010) (proposing CFPB be housed within the FDIC with diminished powers). The final placement of the CFPB within the Fed rather than as its own independent agency was a compromise measure in response to these efforts, but which largely seems to have preserved the independence of the CFPB. *See* Dodd-Frank Act §§ 1012, 1024, 1025 (to be codified at 12 U.S.C. §§ 5492, 5514, 5515).

[52] See, e.g., Dodd-Frank Act §§ 1015, 1025 (to be codified at 12 U.S.C. §§ 5495, 5515).

agencies can petition the FSOC to stay or overturn a CFPB regulation if a conflict with another agency's policies is perceived.[53]

In a similar vein, some scholars have suggested the creation of a dedicated public interest council, an independent governmental entity comprised of experts and public advocates charged with conducting investigations, proposing policies, auditing the regulations proposed and implemented by other financial regulatory bodies, all in an effort to magnify and channel the countervailing interests of citizens to prevent the capture of financial regulatory bodies by sophisticated industry players.[54] Providing such expansive powers for this kind of regulatory agency that acts on behalf of and as a channel for citizen voice is crucial, making these proposals more robust than the ad hoc and more easily ignored current practices of advisory public interest organizations or agency ombudsmen.[55] Creating a dedicated agency in this regard is also superior to a neutral overseeing body like the FSOC, because it is empowered to magnify the political agency of citizens to help balance the terrain of political influence.[56]

Bringing politics back into policymaking

As suggested in Chapter 7 above, regulatory policy decisions are fundamentally political judgments that involve both technical and normative

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[53] Dodd-Frank Act § 1023 (to be codified at 12 U.S.C. § 5513).

[54] Saule Omarova, "Bankers, Bureaucrats, and Guardians: Toward Tripartism in Financial Services Regulation," *Journal of Corporate Law* 37 (2011), 621-674.

[55] Omarova, "Bankers, Bureaucrats, and Guardians," 635-58.

[56] Omarova, "Bankers, Bureaucrats, and Guardians," 673.

considerations.[57] Avoiding these concerns does not remove them, but rather creates the threat of morally-weighty policy judgments being made under cloak of expertise. Furthermore, as the moral stakes get higher, expertise alone cannot bear the weight of justification, and avoiding these moral dimensions creates even greater pressure on the politicization of what expertise can offer.[58] Rather than seeking to sterilize regulatory policymaking of these normative dimensions, agencies should acknowledge more openly that politics, subjective judgments, ambiguity, and uncertainly all create gaps in what expert knowledge can resolve.[59] By embracing these political dimensions and creating a political process to make these judgments, agency policymaking can be transformed into a more democratic political process.

Yet as currently constituted, regulatory agencies are incentivized and structured to resort to technocratic justifications for their policy positions, even when those positions are politically or morally-influenced. Major regulations are subject to two forms of review: first, a review within the executive branch by OIRA, which under Executive Order 12866 is charged with ensuring that regulations pass the test of cost-benefit analysis;[60] and second, a review by the

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[57] See also the discussion in Chapter 10 below.

[58] See e.g., Brown, *Science in Democracy*; Kathryn Watts, “Proposing a Place for Politics in Arbitrary and Capricious Review,” *Yale Law Journal* 119 (2009), 2-85, at 33; and discussion below.

[59] See Martin Shapiro, *Who Guards the Guardians? Judicial Control of Administration* (Athens: University of Georgia Press, 1988), 142-151; Christopher Edley, Jr., *Administrative Law: Rethinking Judicial Control of Bureaucracy* (New Haven: Yale University Press, 1990), 190-9; Cass Sunstein, “Factions, Self-Interest, and the APA: Four Lessons Since 1946,” *Virginia Law Review* 72 (1986), 271-296, at 281.

[60] See Elena Kagan, “Presidential Administration,” *Harvard Law Review* 114 (2001), 2245-2385.

judiciary under the "arbitrary and capricious" standard.[61] In both forms of review, the incentive for agencies is to claim expertise-based foundations for their policies, resorting to technocratic justifications.

Take for example, the 2007 Supreme Court case of *Massachusetts v. EPA*. In this case, the Supreme Court challenged the Environmental Protection Agency's (EPA's) decision under the Bush administration to decline a petition by states requesting new regulations on greenhouse gas emissions under the authority granted by the Clean Air Act. The majority opinion criticizes the EPA for giving insufficient scientifically-based reasons for its denial of the rulemaking petition, arguing that the EPA could not legitimately appeal to the policy priorities of political leaders like the President or his appointed head of the EPA.[62] The decision is thus what Jody Freeman and Adrian Vermeule have called "expertise-forcing": an attempt by the Court to ensure that agencies base their policies on scientific expertise, free from outside political pressures whether from the White House or political appointees.[63] This holding rested on a sense that the EPA had not acted in good faith, and that its policy judgments rested on political imperatives instead:

> Although we [the Court] have neither the expertise nor the authority to evaluate these policy judgments, it is evident they have nothing to do with whether greenhouse gas emissions contribute to climate change. Still less do they amount to a reasoned justification for declining to form a scientific judgment.[64]

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[61] See e.g., *Motor Vehicle Manufacturers' Association v. State Farm Mutual Automobile Insurance Co.*, 463 U.S. 29 (1983).

[62] *Massachusetts v. EPA*, 549 U.S. 497 (2007).

[63] Jody Freeman, Adrian Vermeule, "Massachusetts v EPA: From Politics to Expertise," *Supreme Court Review* 2007(2), 51-110, at 52.

[64] *Massachusetts*, 549 U.S., at 533-34.

While it was the liberal bloc on the Court in *Massachusetts* who turned to expertise to combat what it saw as undue political influence tainting climate science in the Bush administration, this same expertise-forcing approach has hobbled efforts to expand financial regulations even after the passage of Dodd-Frank. The DC Circuit court in particular has a recent track record of being hostile to expanded financial regulations,[65] and has found ways to cast doubt on new regulations pursuant to Dodd-Frank as resting on insufficiently expert justifications.

For example, the Securities and Exchange Commission (SEC) issued a rule on shareholder proxy access to corporate board elections pursuant to Dodd-Frank, only to have the rule struck down on the grounds that agency had offered insufficient empirical evidence that this rule would improve corporate governance. Industry groups challenged the rule arguing that the SEC had inadequately considered the economic impact of the rule, which the SEC is under special obligation to do under statutory language compelling particular attention to considerations of efficiency, competition, and capital formation effects,[66] and under prior DC Circuit precedent.[67] Despite the SEC's stated evaluation of the costs and benefits of its rule, the Court found that the agency had "inconsistently and opportunistically" skewed its cost-benefit analysis, listing several faults such as the failure to quantify certain costs or to adequately justify its predictive judgments.[68]

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[65] See Ben Protess, "Regulator Prepares to Appeal Dodd-Frank Court Ruling," *New York Times*, Dealbook, October 9, 2012.

[66] See 15 USC 78c(f), 78w(a)(2), 80a-2(c).

[67] *Chamber of Commerce v. SEC*, 412 F.3d 133 (D.C. Cir. 2005).

[68] *Business Roundtable and Chamber of Commerce of the USA v. SEC*, No. 10-1305 (D.C. Cir. July 2011), 7.

The agency had provide "insufficient empirical data" on whether the rule would actually create benefits of board performance and increased shareholder value, relying on two "unpersuasive" studies of the subject.[69]

In a similar case, the Commodity Futures Trading Commission (CFTC) issued a new rule on position limits for derivatives trading.[70] The CFTC saw this rule as required by Dodd-Frank's directive that the CFTC prevent "undue burdens" associated with "excessive speculation" regardless of any finding of cost-benefit analysis. The CFTC also argued the rule was a prophylactic one that did not require an affirmative finding that such position limits would be necessary to protect derivatives markets. Industry groups however challenged the rule for being based on insufficient scientific evidence as to the rule's impacts on derivatives markets.[71] The DC Circuit found that the statutory language permitted but did not require the CFTC to issue the rule—and as a result the agency would have to provide a more reasoned justification for its decision on remand.[72]

In all of these cases, courts have deployed their power of reviewing the justifications of regulatory actions under the "arbitrary and capricious review" standard as a way to force agencies to ground their decisions on sufficient scientific evidence. Justifying regulations as resulting from a political command from the executive or the legislature is treated with suspicion by courts in practice This technocratic disciplining of agency justifications has been accepted "uncritically"

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[69] *Ibid.*, 11.

[70] CFTC, Position Limits Rule, 76 FR 71626 (November 2011).

[71] See Protess, "Regulator Prepares to Appeal Dodd-Frank Court Ruling," *New York Times*, October 9, 2012.

[72] *International Swaps and Derivatives Association v US*, ___ F. Supp. 2d ___ (D.D.C. 2012), 2012 WL 4466311.

by judges and scholars alike.[73] Yet this expertise-forcing doctrine tends to operate as a proxy for substantive disputes; rather than actually forcing expertise, the result of this doctrine is to submerge the real dimensions of policy debate beneath a veneer of technocratic justification or judicial oversight. Indeed, judges' ideological and partisan agreement with the substance of agency policies affects their likelihood of upholding agency decisions under arbitrariness review.[74]

The arbitrary and capricious doctrine should be revised to allow greater room for normative as well as technocratic justifications for agency policymaking. This approach would mitigate the danger that courts themselves might use the arbitrary and capricious standard as a pretext for voicing substantive disagreement with agency policies. Further, by openly allowing certain kinds of political factors to weigh on agency policymaking, this shift in arbitrariness review can help remove some of the smokescreen around agency policy judgments: "Encouraging agencies to disclose political factors rather than hiding behind technocratic facades would enable more political influences to come out into the open, thereby enabling greater political accountability and monitoring."[75]

How might political judgments be more brought to the fore in regulatory decision-making? First, the Court could simply require a more explicit statement of the agency's reasons—scientific, technical, as well as political.[76] So long as these

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[73] Watts, "Proposing a Place for Politics," 32.

[74] Richard Revesz, "Environmental Regulation, Ideology, and the DC Circuit," *Virginia Law Review* 83:8 (1997), 1717-72; Cass Sunstein, David Schkade, Lisa Ellman, "Ideological Voting on Federal Courts of Appeals: A Preliminary Investigation," *Virginia Law Review* 90:1 (2004), 301-54; Thomas Miles, Cass Sunstein, "The Real World of Arbitrariness Review," *University of Chicago Law Review*, 75:2 (2008), 761-814.

[75] Watts, "Proposing a Place for Politics", 42.

[76] See e.g. *State Farm*, 463 U.S., Rehnquist dissent.

political judgments are disclosed, and consonant with explicit authorizations such as Congressional statutory language or Presidential Executive Orders, they can be accepted as appropriate judgments.[77]

Second, Congress can facilitate greater normative transparency and contestability by providing more detailed descriptions of the policy goals and evaluative standards in its statutory delegations of agency authority. For example, many environmental statutes require agencies to promulgate regulations that require industries to use "best available technologies," but the statutes do not define what constitutes a best available technology. In light of congressional silence, some cases have interpreted the standard to mean "cost effective technology," but even then it is unclear what level of risk reduction is cost-effective at what price.[78] Congress could instead provide more detailed descriptions of evaluative standards that agencies and courts should employ in formulating and reviewing regulations.[79]

Third, agencies themselves could engage in preliminary rulemakings that focus on establishing the principles or evaluative methodologies that the agency plans to use for a certain set of regulations. For example, agencies could solicit public comments on a particular method of weighing competing values. Similarly, agencies could issue statements that outline the normative or political principles to be used to guide discretionary rulemaking decisions in a particular area of

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[77] Watts, "Proposing a Place for Politics," 45-73.

[78] See e.g. *Entergy Corp. v. Riverkeeper, Inc.*, 129 S. Ct. 1498 (2009).

[79] Such substantive guidance within the statute would also have the added benefit of avoiding pockets of non-reviewable agency discretion where there simply isn't enough statutory language to guide judicial review. See *Heckler v. Chaney*, 470 U.S. 821 (1985).

regulation. These statements could then provide a basis both for direct public engagement through notice and comment, and for possible judicial review if agencies are seen to depart from these regulations themselves.[80]

Fourth, this process of agencies declaring the values or principles guiding their policymaking can be further facilitated and incentivized through presidential administration. As defenders of presidential administration have regularly noted, presidential oversight can function both as a mechanism for promoting policy coherence, and as a way of linking agency policies to the political and democratically accountable goals of the executive.[81] A new Executive Order could amend the regulatory review process requiring agencies to submit such statements of principles and general approach in addition to the current practice of regulatory impact assessments and cost-benefit analyses. Similarly, presidents could issue executive orders that state basic values that will guide the analysis or policymaking of administrative agencies, enforcing these orders through the regulatory review process. Currently, the requirement for agencies to submit cost-benefit analyses is the only institutionally enforced aspect of the range of such executive orders. But it is possible to use the mechanics of presidential oversight to evaluate agency proposals not only for whether they have employed sufficient cost-benefit analysis, but also for whether they have, for example, taking sufficient consideration of other normative policy goals as determined by the president.[82]

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[80] *United States ex rel Accardi v Shaughnessy*, 347 U.S. 260 (1954); *FPC v. Texaco, Inc.*, 377 U.S. 33 (1964).

[81] See Kagan, "Presidential Administration."

[82] Executive Order 13132, for example, requires agencies to take adequate consideration of federalism concerns, calling for additional justification for policies that burden state or local governments. This is a good example of a normative value imposed to shape agency policymaking through the regulatory review process. However, it is also notable that this executive order is not

These reconfigurations of the administrative state are relatively minor, but would facilitate more open normative argument in agency policymaking, placing normative considerations alongside factual and technical ones in policy discourse. This in turn opens up more space for democratic engagement, contestation, and accountability. There may still be incentives for agencies and presidential officials to deliberately clothe decisions in technocratic language to stave off political challenge. But by removing the institutional and legal incentives to do so, these reforms can mitigate this tendency to cover political and normative policy decisions in the aura of pretextual technocratic expertise. Further, by facilitating more open statements of normative policy values, this overall approach helps create the preconditions for more effective democratic engagement. Without a clear understanding of what values are at stake or being employed, it is difficult for many groups to adequately mobilize and engage with the policymaking process—a difficulty that will not be shared by more sophisticated, well-resourced, and well-connected interest groups. Such normative transparency is thus vital to counteract imbalances of representation, influence, and political power.

This effort to bring politics back into regulatory policymaking does not reject the role of agency expertise or policy science altogether. But it does place it on more even footing with other elements that go into policy decisions. Instead of a turn to technocratic discourse that obscures other considerations operating in the background or otherwise narrows the space for citizen engagement with policy

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often enforced the way the cost-benefit analysis provisions of Executive Order 12866 are. A more open and deliberate use of executive orders as mechanisms for articulating and enforcing normative values could also lead to more effective enforcement and coordination as the administration focuses its efforts, rather than attempting to implement a wide range of facially neutral mechanisms that in practice will nevertheless are already inflected with the values of the administration.

debate, expertise is paired with other forms of normative and political argument to enliven and facilitate greater public discourse.

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The regulatory state can therefore be reconstituted not as a domain of technical implementation or technocratic judgment, but rather as a space for participatory, and contestatory, democratic politics. Regulatory agencies already possess relatively broad powers, but much of the current structure of the regulatory state instantiates a technocratic view of regulation—for example, through the requirement of neutral, scientific justifications for policies. By contrast, the suggestions above indicate ways in which the authority of regulatory agencies can be embedded in a more vibrant democratic politics: by engaging citizens more directly through participation and representation; involving citizens not only in the formulation but also in the implementation, enforcement, and revision of policies; and by opening the discourse of justification beyond technocratic expert discourses to engage with the moral and political concerns that are central to regulatory policy. These efforts are particularly vital in economic governance, where the presence of such institutional frameworks for political action is crucial to enable individual citizens to mobilize and act effectively in governing and remaking our economic order.

Reconstituted in this way, the regulatory state can be a crucial forum, catalyst, and enabler of democratic politics. The democratic potential of the regulatory state stems from its position as a 'front-line' institution of governance: a set of bodies that exists at exactly the porous boundary between "the state" on the one hand, and the citizenry on the other. Regulatory agencies are among those

bodies that are charged with crafting, implementing, and adjudicating the final, specified policy initiatives, and thus interact more directly with the world than more removed spaces of policymaking. In a similar manner, democratic agency over the economy can be facilitated through another front-line institution of our democracy: local governments. But where the problem of regulatory agencies was primarily one of organizing an existing broad set of authorities along more participatory lines, the challenge with the local is to harness a greater participatory potential that is undermined by the constrained nature of local regulatory power.

9 DEMOCRACY THROUGH THE CITY

Enabling democratic participation in economic governance is not just a matter of reforming our regulatory institutions at the national level. Much of the day-to-day business of government takes place through local government bodies. These institutions provide another front line in the interface between the state and the citizen. As such, they offer another set of potential spaces for meaningful democratic participation. Although local government bodies are often romanticized as intrinsically linked to grassroots democracy, in practice these institutions rarely meet these aspirations. Where federal regulatory agencies often possess broad powers, but have a structure and process that makes them relatively distant from participation, these local bodies have a different set of problems. Legally, local governments have severely limited powers that undermine their efficacy as democratic forums. Thus, another vector through which democratic agency can be fostered is through the reform of local government institutions to provide them with greater regulatory powers in a way that encourages participation in governance.

The unrealized democratic promise of the city

As with the consolidation of agency authority, there are civic benefits to restructuring the scope of local government power. For all the romantic imagery associated with local democracy, the reality of local democracy is very different. Localities are hobbled by tight legal limits on the kinds of powers they can

exercise—and as a result are limited in the capacity to serve as a viable forum for meaningful democratic participation. Indeed, historically, the same anxieties that have driven both the technocratic and laissez-faire understandings of economic governance—concerns about likelihood of corruption and capture, fears of inefficient government, or anxieties about the use of state power to undermine liberties—have been particularly acute in context of local government. It is because of these concerns that local government has evolved into its current, limited form. Yet in the process, the participatory democratic potential of the locality has been undermined.

The history of local government law has been one of evolving limits and constraints on the powers of municipalities, following many of the same currents that shaped the discourses of economic regulation and the administrative state. Formally, cities, like corporations, are chartered creations of the state legislature. Early American law struggled to categorize and regulate municipal corporations: municipal corporations were publicly chartered like private corporations, but seemed more akin to associations than they did to hierarchical firms.[1] By the eighteenth century, municipal corporations had been distinguished from private corporations: where private corporations required protection from state interference as products of constitutionally- and legally-protected individual property rights, municipal corporations were instead treated as instruments of the state, to be created and constrained as needed to prevent abuses of state power and the problems of faction.[2] Local governments were understood to have only the

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[1] Gerald Frug, "City as a Legal Concept," *Harvard Law Review* 93 (1980), 1057-1154, at 1096-7.

[2] Frug, "City as a Legal Concept," 1099-1106.

authority to act where it is expressly granted by the state legislature. Further, localities were understood as creatures of the state legislature, with no inherent rights or protections of their own.

Just as nineteenth century concerns about the regulatory state cited risks of capture, corruption, inefficiency or unresponsiveness, these same concerns drove the attempt to narrow the powers of municipal corporations. Under what came to be known as Dillon's rule, grants of regulatory power to municipalities were to be read narrowly. Despite earlier practices of state and local level economic regulation for the public welfare, cities were seen as a particularly flawed institutional approach to governance.[3] Dillon's rule and its limited view of the powers of localities stemmed not from an outright rejection of the idea of local democracy, but rather out of a concern about unchecked public power as a threat to property and liberty—and out of a fear that local governments left to their own devices would act irrationally, or be captured by special interests. For some critics of city power, the presumption behind Dillon's Rule was that state oversight of cities would be preferable precisely because state governments would be more rational, effective, and responsive—exemplifying the technocratic vision of regulation.[4] But in practice, Dillon's Rule worked to help foster a laissez-faire political economy, as judges used the presumption against local authority to limit attempts at economic regulation or redistribution, as judges operated under the

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[3] See e.g. David Barron, "Reclaiming Home Rule," *Harvard Law Review* 116 (2003), 2257-2386, at 2283-5.

[4] Frug, "City as a Legal Concept," 1110-2.

same understandings of laissez-faire that shaped critics of the early regulatory state in cases like *Lochner*.[5]

Just as Progressive Era reformers sought to combat laissez-faire thought through creating regulatory agencies and other mechanisms for democratic action, many of these reformers also saw Dillon's rule and its support for laissez-faire political economy as another element of laissez-faire governance in need of reform. In this case, the presumption against local power seemed instead to encourage greater efforts by factions and special interests to capture state legislators, moving the problems of corrupt, or ineffective governance up a level.[6] In response, Progressive Era reformers across the country sought to reinvent the city as a democratic forum.

For many reformers, city-level politics offered a path to realizing democratic aspirations of self-rule and self-government.[7] The social and economic problems of an industrializing economy were most visible in the city, with its concentrations of poverty, social fragmentation, and extreme inequalities of wealth.[8] At the same time, cities were the primary providers of social services, housing, sanitation, and other central services.[9] Cities offered the promise of an alternative democratic space where the citizenry could be empowered to make public policy free of the

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[5] Barron, "Reclaiming Home Rule," 2285.

[6] Barron, "Reclaiming Home Rule," 2286-8.

[7] Daniel Rodgers, *Atlantic Crossings: Social Politics in a Progressive Age* (Cambridge: Harvard University Press, 1998), 158.

[8] Rodgers, *Atlantic Crossings*, 112-3.

[9] See Richard Schragger, "The Progressive City," in Kathleen Claussen, Adam Grogg, and Sarah Russell, eds., *Why the Local Matters: Federalism, Localism, and Public Interest Advocacy* (New Haven: Yale Law School, 2008), 39-50, at 40-4.

constraints of the judiciary, and of party bosses and special interests dominating state legislatures. But in order to fully realize these reformist aspirations, local government itself had to be reformed to overcome patterns of corruption and party boss rule.[10]

Thus, a number of reformist movements emerged with the goal of facilitating deliberation, community, and political engagement within the city. The "city beautiful" movement led by organizations like the American League for Civic Improvement and the American Park and Outdoor Art Association sought to engineer public spaces aimed at provoking local pride, social interactions, and deliberation.[11] Frederick Howe led reformers and reformist politicians in Cleveland and New York to develop systems of local forums aimed at bringing citizens together with elected officials and policymaking experts, in order to displace the political power of corrupt parties.[12] This turn to the city as a forum—from the establishment of city utilities to the brief anti-chain store movement—there was a link between an empowered locality as a political space, the ability of citizens to experience real democratic agency and self-government, and the capacity to experiment with new policies, particularly in responding to the upheavals of the new industrial economy.[13] While some activists and thinkers emphasized harmony and community as the key goals, others focused more centrally on the task of

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[10] Rodgers, *Atlantic Crossings*, 156-9.

[11] Keith Mattson, *Creating a Democratic Public: The Struggle for Urban Participatory Democracy During the Progressive Era* (University Park: Pennsylvania State University Press, 1998), 16-30.

[12] Mattson, *Creating a Democratic Public*, 32-47.

[13] See e.g. Richard Schragger, "The Anti-Chain Store Movement, Localist Ideology, and the Remnants of the Progressive Constitution, 1920-1940," *Iowa Law Review* 90 (2005), 1011-1094, especially 1082-5.

encouraging political judgment and democratic deliberation through increased social interaction, argument, learning, and engagement with the day-to-day practice of urban governance.[14]

The biggest policy success of these efforts came in the Home Rule movement. Through state constitutional amendments that guaranteed city authority to make policy on "local" policy issues, Home Rule would promote of public good by creating an alternative space for policymaking apart from corrupt state legislatures, while also imposing a set of legal authorities and constraints that would encourage good government at the local level.[15] In practice, however, the legacy of Home Rule as a democratizing innovation has been mixed. Home Rule paradoxically has operated as much as a constraint on localities as an empowerment of them.[16]

In current practice, municipalities do enjoy the autonomy to make public policy under Home Rule provisions, but face two major constraints on this authority. First, there continues to be an ongoing legal and judicial debate over what counts as a matter of "local" concern where Home Rule powers apply. While many states have Home Rule amendments granting local governments some form of autonomy, local efforts to experiment with new social and economic policies such as gun control, local campaign finance, minimum wage laws, rent control, and mortgage regulations are often found preempted by state or federal authority,

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[14] Mattson, *Creating a Democratic Public*, 69-77.

[15] Barron, "Reclaiming Home Rule," 2289-91.

[16] See e.g. Frug, "City as a Legal Concept," 116; Barron, "Reclaiming Home Rule," 2290; Frug and Barron, *City-Bound: How States Stifle Urban Innovation* (Ithaca: Cornell University Press, 2008), 36-8.

on the grounds that these city policies implicate policy decisions that are not purely local, and where federal or state authorities trump the locality.[17] The viability of localities as forums for democratic action is undermined when localities are viewed as having narrowly limited domains of authority. These disputes underscore that the attempt to demarcate city authority on the basis of a distinction between "local" and "national" subject matter is a shaky approach to city level democracy at best.[18]

Second, local authority is also circumscribed by the competing authority of neighboring localities. Ironically, by granting autonomy to all localities, the structure of Home Rule creates tendencies towards fragmentation and policy competition: the ability of one locality to enact regulations on business or economic development efforts, for example, is constrained by the degree to which other neighboring localities enact rival policies that run in a different direction.[19] This problem is compounded by the fact that many local areas are actually governed by dozens, sometimes hundreds, of distinct municipal corporations; the greater Boston metropolitan region for example, is actually comprised of several hundred rival, and autonomous, municipal bodies.

These limitations to Home Rule as a legal guarantor for local level democracy were embedded from the beginnings of the Home Rule movement. Despite its apparent commitment to local autonomy and local-level democracy, the

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[17] See e.g. *New Orleans Campaign for a Living Wage v. City of New Orleans*, 825 So.2d 1098 (2002); *Town of Telluride v. Lot Thirty-Four Venture*, 3 P.3d 30 (Colo. 2000); *American Financial Services v. City of Oakland*, 34 Cal.4th 1239 (2005).

[18] Frug and Barron, *City-Bound*, 61.

[19] Frug and Barron, *City-Bound*, 39-41; 206-9.

Home Rule movement was largely driven by the same concerns for good governance that has shaped the historical debates over economic regulation and the administrative state. As a result, reformers often saw their task not as *enabling* governmental power, but rather as *constraining* it to prevent irrational or illiberal policies. Again, the debate revolved around a clash between technocratic, laissez-faire, and democratic understandings of city power. The debate during the turn of the twentieth century over local power thus revolved around the same triad of conceptions of political economy that animated similar debates over economic governance and regulation: laissez-faire, technocratic, and democratic.

Thus, the Home Rule movement gained ground in the turn of the twentieth century precisely because the idea of Home Rule "served as a placeholder for an array of conflicting concrete proposals," winning support from both conservative defenders of laissez-faire and Progressive proponents of technocratic expertise.[20] For the conservatives, Home Rule offered a technique to limit the growth of taxation, spending, and governmental power more generally. By defining a narrow scope of local power in a state constitutional amendment, these reformers could limit the ability of state legislatures to manipulate city policies and structures in response to special interest lobbying. Home Rule would also restore the ideal of small government focused solely on minor local issues rather than larger visions of social reform. In so doing, these conservatives hoped, as similarly-minded thinkers in other contexts like the *Lochner* decision, to preclude the risk of "special

[20] Barron, "Reclaiming Home Rule," 2291. See also Frug and Barron, *City-Bound*, 36-8.

legislation" favoring particular factions, or other forms of state capture or corruption.[21] As David Barron explains,

> finding neither local autonomy nor its opposite attractive, the old conservatives pursued a middle path. They sought to rejigger the city- state legal relationship in a way that would restore the idealized small- scale, low-tax, low-debt, highly privatized (and thus incorruptibly public) ideal of local government that seemed on the verge of being lost forever.[22]

Technocratic Progressives had a very different ideal vision of government—not the small, noninterventionist government of the laissez-faire advocates, but rather an expert-based administrative government capable of developing complex social policies—but they shared the conservative anxiety over corruption, capture, and inefficiency. Home Rule, for these technocratic reformers, offered a way to rationalize state policy, specifically by pairing local autonomy with extensive *administrative* rather than legislative oversight by the state.[23] As with their contemporaries advocating for the rise of the federal regulatory state, these reformers saw technocratic expertise as the ideal way to defuse the anxieties of critics like Dillon, without abandoning the idea of economic regulation and the ability of localities to respond to social problems altogether.

The historical advocates for Home Rule saw it as a way to rationalize and constrain—rather than truly empower—local government. It is no surprise, then, that localities continue to struggle to enjoy the kind of powers and authority necessary for them to serve as viable forums for democratic political agency. Yet there was a third vision of local power present in the Home Rule movement. This

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[21] Frug and Barron, *City-Bound*, 37.

[22] Barron, "Reclaiming Home Rule," 2294.

[23] Frug and Barron, *City-Bound*, 37; Barron, "Reclaiming Home Rule," 2300-7

third batch of reformers had a very different motivation: focused not on the need to *constrain* problematic exercises of state power, but rather on the need to *catalyze, enliven, and enable* the political power of citizens as makers of their own collective futures. For these reformers, the locality was seen primarily as an expression of the shared social experience of citizens aspiring towards self-government—rather than being a way to protect private property or to promote administrative expertise:[24] "The benefits of Home Rule were to be found in the political effect of arousing a public realm too long dominated by private power, rather than in the promotion of administrative or business-like efficiency."[25]

These reformers thus sought to expand the locality's policy capacity, enabling it to engage in big policy issues of the day, through expanded powers to tax, regulate activities, and even to operate utilities.[26] In contrast to the Home Rule focus on matters of "local" concern, these reformers saw the local not as a particular set of issues, but rather as a *forum* through which citizens could experience self-government on issues of central concern, including major national issues.[27] This vision of the democratic city thus follows the strand of radical democratic Progressivism espoused by thinkers like Dewey and Brandeis—and like those thinkers, sought to respond to the problems of capture, corruption and inefficiency neither through privatization nor expertise but rather through mechanisms to empower greater democratic self-rule. As Frug argues, "cities have

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[24] Frug and Barron, *City-Bound*, 38.

[25] Barron, "Reclaiming Home Rule," 2309.

[26] Barron, "Reclaiming Home Rule," 2312-8.

[27] Barron, "Reclaiming Home Rule," 2310-11.

served—and might again serve—as vehicles to achieve purposes which have been frustrated in modern life," especially by realizing "the ability to participate actively in the basic societal decisions that affect one's life."[28] This defense of local power is distinctive; the local is valuable, in this view, *not* because it enables a diversity of localities that cater to individual preferences, nor because it speaks to matters of purely local concern, but rather because it offers a space in which citizens can experience meaningful political agency as they attempt to respond to the social problems of the day. This is the kind of participatory vision that is needed to reformulate the balance of local power today.

Today, the problem of local powerlessness erodes the potential for this participatory vision.[29] Whether in the form of Home Rule constraints, Dillon's Rule, or further limitations arising from the narrow tax base, limited tax authority, localities are tightly constrained in their ability to enact public policy.[30] Municipal corporations have even less power to act than private corporations, despite their shared ancestry.[31] Even where city-level democracy seems secure within limited areas of city power, the prevailing democratic skepticism of the era hollows out further the scope for democratic participation at the local level. Many city functions are now provided by alternative technocratic bodies, special districts, and

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[28] Frug, "City as a Legal Concept," 1068.

[29] Frug, "City as a Legal Concept," 1072.

[30] See e.g. Frug and Barron, *City-Bound*; Frug, "City as a Legal Concept," 1062-4.

[31] As Frug notes, city discretion is the application of coercive power to liberty and must be restrained, while corporate discretion is the exercise of that liberty and must be protected." See Frug, "City as a Legal Concept," 1066.

public-private partnerships, over which cities themselves have little control.[32] As we have seen elsewhere, the pattern is a consistent one of institutionalizing constraints on political action, either because the idea of participatory democracy seems "so bizarre, so dangerous, and so unworkable that most state constitutions prohibit its emergence," or because the notion of city discretion of any kind "evokes images of corruption, patronage, and even foolishness."[33]

Localism and democratic economic governance

The value of cities as democratic spaces—and their relative weakness in contemporary policymaking, particularly on economic matters—is well exemplified by the role of local governments in anticipating the financial regulation debate. Cities were at the forefront of identifying and attempting to respond to the emerging subprime lending crisis. But the current structure of local power stymied efforts by citizens and localities to respond to the subprime lending and financial crisis.

Predatory lending was a major cause of the financial crisis, as borrowers found themselves caught in subprime mortgage loans which they could not repay, leading to waves of foreclosures that decimated many communities and eventually undermined the value of a wide array of mortgage-backed securities. Predatory lending refers to loans and lending practices that include characteristics such as excessive fees, excessive interest rates, lending without regard to the borrower's

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[32] Frug, "City as a Legal Concept," 1065-6. See also Richard Briffault, "Who Rules at Home: One Person/One Vote and Local Governments," *University of Chicago Law Review* 60 (1993), 339-424.

[33] Frug, "City as a Legal Concept," 1073, 1066.

ability to repay, loan flipping, fraud and deception, prepayment penalties, and balloon payments.[34] As early as 2000, a range of community advocacy groups in multiple states appealed to federal regulators such as the Office of Thrift Supervision (OTS) to crack down on predatory lending, while hard-hit cities such as Cleveland lobbied Federal Reserve to regulate the industry more stringently.[35] These appeals ultimately were not followed. Federal regulators systematically undercut state and local efforts to regulate predatory lending during the 2000s, in the lead up to the financial crash.

A number of municipalities took the lead in attempting to regulate predatory lending through city ordinances. But such local ordinances passed in almost 20 cities faced near immediate preemption challenges.[36] In California, the city of Oakland adopted a local ordinance regulating lending and home mortgages. A few days later the California legislature passed its own predatory lending law. The financial services industry promptly challenged the more stringent Oakland ordinance, arguing that California state legislation had occupied the field of mortgage lending regulation, thereby preempting the Oakland ordinance. California courts ultimately agreed, ruling against the city of Oakland.[37] While the

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[34] Jonathan Entin, Shadya Yazback, "City Governments and Predatory Lending," 34 *Fordham Urban Law Journal* 757 (2007), at 760-1, quoting US GAO, Consumer Protection: Federal and State Agencies Face Challenges in Combating Predatory Lending (2004), http://www.gao.gov/new.items/d04280.pdf

[35] Financial Crisis Inquiry Commission (FCIC), *The Financial Crisis Inquiry Report* (New York: Public Affairs, 2011), 10.

[36] Entin and Yazback, "City Governments and Predatory Lending," 771-2.

[37] *American Financial Services v. City of Oakland*, 34 Cal.4th 1239 (2005). Oakland passed a publicly-backed municipal code regulating the subprime industry and the secondary mortgage market. However, local area banks opposed the measure, and successfully combined with other groups to help push through a state level regulatory statute that specified less-stringent regulations. These banks then initiated a lawsuit to strike down the Oakland regulation as preempted by (i.e. inconsistent with) the state statute. Though Oakland argued that it had the authority to pass

state law did not include any express preemption language, it exhibited an "implicit intent to fully occupy the field of regulation".[38] Oakland's local concerns with blight and foreclosures "do not give the City a license to regulate a highly complex financial area comprehensively addressed by state law."[39] Yet as the dissent in the case noted, the question of local preemption was explicitly considered and rejected by the state legislature, despite a push by the same industry groups bringing the lawsuit itself.[40] Oakland could rightly have considered its ordinance a local community development measure. Furthermore, the ordinance did not contradict the state law, instead providing additional borrower rights not covered in the state law, in effect furthering rather than subverting the state law's intent of protecting low-income borrowers.[41]

This pattern—where economically distressed cities attempted to revive their communities by regulating predatory lending, but were thwarted at the state level as the financial industry pursued state legislation and preemption through state courts—repeated itself across the country. In Ohio, the city of Cleveland passed its own anti-predatory lending ordinance which was intended to build on existing state predatory lending laws. In response, national financial institutions fled the city, while the state legislature pursued litigation to eliminate the ordinance. In

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regulations that went above and beyond the minimum floor established by the state statute, the court ruled that the state regulation set both a minimum and maximum level of regulation, and struck down the Oakland code. It should be noted that the state statute was ultimately relatively weak in its impact on banks.

[38] *AFSA v. Oakland*, 34 Cal.4th, at 1252.

[39] *AFSA v. Oakland*, 34 Cal.4th, at 1259.

[40] *AFSA v. Oakland*, 34 Cal.4th, at 1266-7.

[41] *AFSA v. Oakland*, 34 Cal.4th, at 1273.

litigation backed by the same financial services industry group that challenged the Oakland ordinance, the Ohio Supreme Court found the Cleveland ordinance unconstitutional for attempting to regulate matters of general statewide concern, thereby going beyond the scope of municipal powers and conflicting with the prerogative of the state legislature.[42] The Supreme Court also invalidated a similar effort by the city of Toledo.[43] Similarly, New York City also attempted to push back against predatory lending through its Local Law 36, which stipulated that the city would only contract with vendors who did not engage in predatory lending or work with predatory loans. Although the city possessed discretion over "proprietary laws" which involved the city's own dealings with its vendors, New York state court found Local Law 36 to be a thinly veiled "regulatory law", beyond the scope of the city's power, and preempted by state banking law.[44]

In addition to passing local ordinances, several cities attempted to use the courts as litigants to change state and federal regulations in an attempt to crack down on predatory lending. But here too, municipalities faced an uphill battle in securing standing to make claims in court. For example, Cleveland attempted to sue Wall Street for public nuisance, arguing that the securitization of subprime mortgages led to foreclosures that cost the city and police and fire expenditures, and to the detriment of the overall public good. But this litigation attempt was also

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[42] *American Financial Services Association v. City of Cleveland*, 824 NE 2d 553 (Ohio Ct App 2004), rev'd 858 NE2d 776 (Ohio 2006). See also, Kyle Cutts, "City on the Brink: The City of Cleveland Sues Wall Street for Public Nuisance" *Case Western Reserve Law Review* 58 (2007), 1399-1421, at 1409.

[43] See *American Financial Services Association v. Toledo*, 830 N.E. 2d. 1233 (Ohio App 6 Dist 2005)

[44] See *Mayor of City of New York v. Council of City of New York*, 780 N.Y.S. 2d., 266 (2004), preempted by NY Banking Law, § 6(i).

defeated on insufficient standing and proximate causation grounds.[45] Further, as one recent analysis suggests, it is unlikely that cities will be able to establish sufficient standing to as *parens patriae* in cases brought in the name of the public interest.[46]

State governments enjoyed some more success in regulating predatory lending, but they too ultimately faced federal preemption that favored the financial services industry. State attorneys-general in Minnesota, California, Washington, Arizona, Florida, New York, and Massachusetts all pursued legal allegations against subprime lenders for fraud and violations of consumer protection laws.[47] Massachusetts, for example, has an extensive consumer protection statute that limits unfair lending practices. This statute was successfully used by the state Attorney General to prosecute banks engaged in subprime lending, and win legal protections for subprime mortgage owners.[48] Other state legislatures such as Minnesota and New York have passed financial regulation statutes.[49] Historically, states have used their police powers to regulate mortgages during times of economic crisis.[50]

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[45] Cutts, "City on the Brink".

[46] See Entin and Yazback, "City Governments and Predatory Lending," 763-4.

[47] See FCIC, 11-12; Frug and Barron, *City-Bound*, 196.

[48] Commonwealth v Fremont Investment and Loan, 897 N.E. 2d 548 (Mass., 2008).

[49] See Minn. Stat. §§ 58.13(1)(a)(24) – (26); NY Banking Law § 6 (g) – (m).

[50] See e.g. *Home Building and Loan association v. Blaisdell*, 290 U.S. 398 (1934) (upholding the constitutionality of Minnesota mortgage moratorium act, which authorized courts to extend periods of redemption for mortgages); *Bank of Craig v. Hughes*, 398 N.W.2d 216 (upholding Iowa code protecting farmers from loss of farms in economic crisis).

But in the 2000s, such state efforts were also preempted by federal agencies. The OTS and the Office of the Comptroller of the Currency (OCC) each issued rulings in 2003 and 2004 intended to occupy the field of predatory lending regulations, interpreting their authority under the National Banking Act to formally preempting state and local efforts in the area.[51] While a number of states, particularly North Carolina, pushed ahead with their own legislation despite this action, resistance by the American Banking Association ultimately culminated in a Supreme Court ruling that construed the National Banking Act protect banks from state regulations even for state-level subsidiaries, effectively siding with the OCC and the OTS against state regulatory efforts.[52]

During the 2000s, city and state governments thus were on the leading edge of identifying the problem of predatory lending and attempting to respond through local regulation. However both cities and states faced barriers to their policies in the form of state and federal preemption doctrines, which were used to great effect by the financial services industry seeking to challenge these more stringent experiments with regulation. Of course, there is no guarantee that state and local governments will always innovate in constructive or socially desirable ways. There will be times when the stated goals of preemption—maintaining coherent and uniform regulations—do apply. However, a more permissive preemption regime would open up state and local governments as spaces where citizens and advocacy groups might be able to adopt regulatory approaches that may otherwise be

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[51] Raymond Brescia, "Part of the Disease or Part of the Cure: The Financial Crisis and the Community Reinvestment Act," *South Carolina Law Review* 60 (2008), 618-677, at 650; Entin and Yazback, "City Governments and Predatory Lending," 780-81.

[52] See FCIC, 13; *Watters v. Wachovia Bank,* 550 U.S. 1; Brescia, "Part of the Disease or Part of the Cure," 650-51.

blocked at the federal level. Further, such a more varied approach could combine federal minimum standards with scope afforded for state and local governments to develop more tailored approaches that go beyond those standards.

Since the 2008 crisis, while there has been some attempt at loosening the constraints on local power, these efforts have not gone far towards institutionalizing the locality as a democratic forum. For example, the Dodd-Frank legislation provides for federal and state interaction on mortgage, insurance, and municipal securities regulations, enabling states to go beyond the minimum standards established by federal regulators.[53] In addition, after extensive debate over the degree of the new Consumer Financial Protection Bureau's (CFPB's) preemption power,[54] the final bill allows states to experiment with consumer protections beyond the minimum standards established by the CFPB. While the CFPB has independent rulemaking authority, it is required to commence a proposed rulemaking when a majority of states pass resolutions in favor of additional consumer protection.[55] In addition, the Supreme Court seemed to support greater leeway for states, holding in 2009 that the OCC's attempt to prohibit state regulations of national banks exceeded its authority under the

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[53] *See* Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, tit. V, subtit. A & B, 124 Stat. 1376 (2010) (to be codified in scattered sections of 15 U.S.C.).

[54] For example, Senators Tom Carper (D-Del.), Mark Warner (D-Va.), Tim Johnson (D-S.D.), and Evan Bayh (D-Ind.) pushed for greater federal preemption power over states on consumer regulation. See Silla Brush, "Centrist Senators Push for Greater Federal Power in Consumer Regulations," *The Hill* (May 11, 2010), http://thehill.com/homenews/senate/97353-centrists-push-for-more-federal-power-in-consumer-regulation. By contrast, Republicans like Senator Bob Corker (R-Tenn.) attempted to bar state attorneys general from enforcing CFPB rules, but his amendment was rejected 43-55. S. Amdt. 4034, 111th Cong. (2010).

[55] Dodd-Frank Act § 1041 (to be codified at 12 U.S.C. § 5551).

National Banking Act.[56] Dodd-Frank explicitly attempts to limit preemption to cases of explicit conflict between local and federal regulators.[57] Yet in 2011, the OCC issued a letter stating that it viewed its preemption rulings as unaffected by Dodd-Frank, despite the new provisions for consultation with state and local authorities incorporated into the bill.[58] But in the early going, courts have struggled to implement this directive clearly, in some cases deferring to the OCC preemption of state regulations,[59] while upholding the state regulations in other cases.[60]

Public law and the revival of the city as participatory forum

The experience of local governments in financial regulation underscores the importance of expanding the role of the local as a space for democratic politics, particularly on matters of economic governance. Achieving this democratic vision requires reformulating the law of local government. Four areas in particular stand out. First, promoting this kind of local democratic experimentalism would require a looser legal doctrine of preemption under both state and federal law. Second, this vision of the local requires a different view of how the federal government relates to the local, including a rethinking of our traditional views of federalism. Third, localities should be granted greater legal standing to make their own claims in

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[56] *Cuomo v. Clearing House Association*, 557 U.S. 519 (2009).

[57] Dodd-Frank, § 1044(a), codified at 12 USC 25b(b)(5)(A).

[58] Comptroller of the Currency, letter to Senator Thomas Carper, May 12, 2011 [on file with author]. Dodd-Frank explicitly attempts to limit preemption to cases of explicit conflict between local and federal regulators. Dodd-Frank, § 1044(a), codified at 12 USC 25b(b)(5)(A).

[59] *Baptista v. JPMorgan Chase Bank*, 640 F.3d 1194 (11th Cir. 2011).

[60] *Cline v. Bank of America*, 823 F. Supp. 2d 387 (SD WV 2011).

court and in national policymaking institutions. Finally, localities should be organized into regional bodies that can coordinate policies and enable further democratic participation and debate across localities experiencing similar shared problems.

Permissive preemption

As noted above, much of local authority is constrained by state and federal preemption, where the local policy is overridden either by an explicitly contrasting policy from a higher state or federal authority, or by an implied conflict between the claim to local authority and the degree to which state or federal governments appear to have already occupied the topical field. Preemption doctrines nominally seek to preserve higher order authority from eroding in the face of competing policies passed by local bodies, thus assuring uniformity and state or federal power. Doctrine nominally seeks to preserve national authority for national issues as distinct from "local" ones, yet "there is no natural order dividing topics into those that are local and those that are not."[61] As a result, preemption doctrine is easily manipulated to prevent local policymaking as a proxy for more substantive policy disputes. Indeed, often, preemption doctrine offers a route for business interests to quash local level experimentation on everything from gun control to minimum wages.[62] Indeed, the risk of a policy patchwork is often overstated: most local governments are cautious, and remain constrained by political forces, public

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[61] Frug and Barron, *City-Bound*, 49.

[62] See Schragger, "The Progressive City," 47-8.

opinion, and economic leverage of businesses, even absent the legal constraint of preemption.[63]

Preemption thus works less to assure policy rationality, and more to erode the idea of democratic empowerment: “The federal judiciary has become a primary facilitator of citizen dis- empowerment by its failure to reconsider and revise existing preemption standards, and by its approval of a wide range of tenuous federal preemption claims.”[64] Preemption doctrine is so broad that any local or state law is potentially open to displacement, thus discouraging innovation and participation, promoting the interests of large national corporations, and conducing to regulatory vacuums.[65]

The aspiration for cities as democratic forums requires that localities possess freer reign to experiment with new policies, rather than being preempted.[66] Preemption doctrine should instead be construed more permissively, to focus on enabling greater citizen engagement and facilitating voice. By granting more scope for local governments to engage in policy development, a more permissive preemption doctrine can encourage greater local policymaking—and this expansion of local power in turn can make local level civic engagement more meaningful. Concerns about irrationality, capture, or ineffectiveness remain, but rather than using these concerns to preclude local power, these concerns can be

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[63] Schragger, “The Progressive City,” 48.

[64] S. Candice Hoke, “Preemption Pathologies and Civic Republican Values,” *Boston University Law Review* 71 (1991), 685-768, at 698.

[65] Hoke, “Preemption Pathologies,” 711-19.

[66] See e.g. State v. Hutchinson, 624 P.2d 1116 (Utah 1980); New Mexicans for Free Enterprise v. City of Santa Fe, 138 N.M. 785 (2005).

met by combining expanded local authority with greater coordination across localities via federal and regional arrangements.

Federal-local linkage

The democratic approach to harnessing local governments in regulatory policy debates can be further encouraged by restructuring the relationship between federal and local policymaking. Current legal doctrine largely calls into question the ability of the federal government to engage in cooperative and coordinated policy schemes with local governments. Such schemes, according to the Supreme Court, may raise concerns that local governments are "commandeered" to execute policies against their will.[67]

While this anti-commandeering doctrine correctly identifies the importance of values such as local autonomy and clear channels of accountability, these values are ironically undermined by the doctrine itself. The doctrine envisions respect for local democracy in terms of protecting a sphere of local sovereignty that is otherwise inviolable. It also focuses more on state sovereignty than on locality per se. As a result, this approach both ignores the importance of local forums below the state level, while also inhibiting the scope for federal-local cooperation.

Indeed, often federal engagement with local forums and institutions can facilitate rather than inhibit the broader democratic vitality of the polity. The integrity of local governmental forums and accountability of public policy to citizens can both be better facilitated by regulatory schemes that combine federal-

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[67] See *Printz v. United States*, 521 U.S. 898 (1997); *New York v. United States*, 505 U.S. 144 (1992).

level resources and expertise with local-level enforcement and citizen engagement. Federal agencies can devise overall policy approaches, harnessing the financial and technical resources of the federal government that many localities lack. But these policies can then be crafted to allow for a range of local-level variation, adaptation, and experimentation, while also harnessing local forums as channels for democratic participation. The Obama administration took some tentative steps in this direction, encouraging local governments to engage with federal agencies to share experiences, ideas, and identify problems.[68] But a more structured approach can be pursued, through statute or executive order.

Democratic regionalism

In addition to harnessing existing local governments, the scope for democratic engagement in regulatory policy can be further expanded by use of additional regional scale policy forums. For example, many regions share common socioeconomic challenges or are interlinked in a dense metropolitan area that cuts across several localities, but is smaller than the state itself. In these settings, neither the state nor the local government matches the scale of the region or its policy challenges. Here, regional bodies can be created—for example, by statute—to address common policy questions to these identifiable regions.[69]

The idea of regional governance has been a recurring one. Massachusetts experimented with regional coordination of localities as early as 1896. In the mid-twentieth century, St. Louis and Cleveland made similar attempts, while the US

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[68] See the Partnership for Program Integrity, http://www.whitehouse.gov/open/partner4solutions.

[69] See generally, Frug, *City-Making*; Frug and Barron, *City-Bound*, 45-50.

Advisory Commission on Intergovernmental Relations proposed a two-tier approach of local and regional governance.[70] Indeed, many states have already created numerous regional and "special district" policy entities aimed at governing a particular policy area—such as water management or mass transit—that concerns a region cutting across several localities.

Today, regional arrangements often exist in areas like environmental management, water utilities, and transportation infrastructure. Yet these entities are often constructed out of the same kind of technocratic considerations that animate national administrative and regulatory bodies: they are deliberately insulated from democratic politics, purportedly to ensure expert-based policymaking. Yet they often function with little meaningful oversight, despite their exercise of significant governmental authority that directly affects many citizens.[71] These entities offer a useful starting point for regional governance—but should be reformulated along more democratic and participatory lines.

More broadly, the multiplicity of localities can be consolidated into more meaningful regions or sub regions that encompass the whole of a particular geographic community. Currently the structure of local government law conduces to greater fragmentation through permissive incorporation regimes and difficult annexation requirements, conducing to the multiplication of municipalities. While multiple local spaces can be helpful for democratic politics, as noted earlier there is a balance to be struck between the idea of consolidation—which assures a single, visible, and empowered governance body that speaks to a particular issue or

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[70] Frug and Barron, *City-Bound*, 46-7.

[71] See e.g. *Salyer Land Co v. Tulare Lake Basin Water Storage District*, 410 U.S. 719; *Ball v. James*, 451 U.S. 355 (1981).

constituency—and the idea of fragmentation, which multiplies spaces to facilitate access. From the standpoint of facilitating democratic voice, localities should be reorganized to track the actually experienced borders of communities of interest—for example, encompassing a metro area.

Municipal standing

Consolidating the borders of localities to track the actually experienced boundaries of affected communities will help empower citizens by giving them a voice within the community of interest that shapes their experience of the local. But by defining a geographically-rooted set of citizens in this way, localities can also help foster democratic voice through another channel: as channels for representation and assertion of the geographical community's collective interests in other policymaking institutions. When other institutions, including courts, federal administrative agencies, and Congress, are deciding issues, there is a value to representation of interests as a locality, rather than through direct citizen engagement with these larger institutions. The locality can channel a different set of collective interests and concerns that may not be captured by individual standing.

Consider for example the recent Supreme Court case of *Massachusetts v. EPA*.[72] The state of Massachusetts, alongside other states, brought suit to challenge the Environmental Protection Agency's (EPA's) denial of a rulemaking petition proposing greenhouse gas regulations. The Court ultimately held that EPA would have to provide scientifically-grounded reasons for its refusal to

[72] *Massachusetts v. EPA*, 549 US 497 (2007).

regulate greenhouse gases under the Clean Air Act. While the biggest impact of the case—as will be discussed in the next chapter—stems from its commitment to expertise as a driver of regulatory policymaking,[73] before reaching the merits, one of the issues in the case concerned the ability of Massachusetts to have standing on this issue. The majority opinion held that states have broad standing rights to bring claims against regulatory agencies—particularly as a form of legal check on the broad powers that agencies exercise, as implied by Congress' guarantee of judicial review of agencies for arbitrary and capricious action.[74] Indeed, Stevens argued that States have long been recognized as having an "independent interest" in its own land, air, and environmental conditions sufficient to generate the necessary adversarial relationship for judicial standing.

The dissent, penned by Chief Justice Roberts, challenged states' standing on the traditional grounds that the parties could not show the a harm that was traceable to the defendant and redressable by the court, largely because of the dissent's view that the state of climate change science was too murky to assign clear lines of causality and blame.[75] But it is interesting to note that Roberts' other argument against standing in the case was a principled stand against standing as states themselves: Roberts argued that climate change was a policy issue to be settled through ordinary legislative channels, and that states ought to channel their concerns through the political arena of Congress or the Executive rather than being

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[73] Jody Freeman, Adrian Vermeule, "Massachusetts v EPA: From Politics to Expertise," *Supreme Court Review* 2007(2), 51-110, at 68-70 (noting that the majority's ruling on the standing issue is relatively straightforward, borrowing from Kennedy's concurrence in *Lujan* in order to move quickly to the merits of the case and the majority's emphasis on expertise).

[74] *Massachusetts*, 549 US 516-26 (Stevens majority opinion).

[75] *Massachusetts*, 540-2 (Roberts, dissenting).

represented directly in courts.[76] Roberts rejected Stevens' argument "special solicitude" of states as litigants, arguing that there were no quasi-sovereign interests at stake sufficient to justify state standing.

The clash between Roberts and Stevens here is telling. We are indeed accustomed to thinking of geographically-based interests as already represented through geographically-rooted districts that elect legislators. But electoral districts rarely if ever coincide with the boundaries of the locality, or of the actually-affected community of citizens. And where it does, as in the case of US states, the geographical units themselves rarely have representation *as collective bodies*. The same problem arises in more severe context for localities, who lack the channel of the federal Senate that states enjoy. As we shall below, cities face difficulties in bringing suits to assert their interests qua cities—as geographically and sociologically determined spaces that have collective interests not easily captured by an individual plaintiff, nor easily channeled politically through district-based legislators. In administrative and legislative bodies, such locality standing can be achieved through the kinds of coordinating and consultation provisions noted above. But legally, localities often face difficulty in asserting their standing *as localities*.

Democratic agency as initiative, not autonomy

There is a vast literature extolling the virtues of federalism as a way of fostering more local participation, accountability, and policy experimentation.[77]

[76] *Massachusetts*, 536-9 (Roberts, dissenting).

These same arguments are better applied to local government bodies, as more local spaces where citizens can participate and governments can innovate policy approaches. Local governments comprise "counterpublics"—forums where citizens can participate, new ideas can be initiated, and problematic regulatory approaches in other jurisdictions can be challenged with alternatives.[78] Multiplying the arenas for policymaking and debate in this way may also help overcome blockage or capture of the regulatory process by providing alternative spaces for initiative or experimentation.[79] Yet, in much of public law doctrine, the locality as a political forum is treated with suspicion and ambivalence. While values of local democratic participation, experimentation, and local tailoring of policies are celebrated, they are often done so in reference to federalism of the state governments.[80] Conservative jurists in particular have sought to bolster the protections for state sovereignty against assertions of federal power.[81] In place of the technocratic and laissez-faire unease with localities as creating a chaotic patchwork of regulations or as conducing to unreflective local passions, the locality can be better viewed as a vehicle for enabling democratic engagement and experimentation.

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[77] See e.g. Yair Listoken, "Learning through Policy Variation," *Yale Law Journal* 118 (2008-9), 480-553; Brian Galle and Joseph Leahy, "Laboratories of Democracy? Policy Innovation in Decentralized Governments," *Emory Law Journal* 58 (2008), 1333-1400 (suggesting that decentralization and policy experimentation at different levels of governance can be beneficial in some situations, whereas national policies may be desirable in others).

[78] See Nancy Fraser, "Rethinking the Public Sphere: A Contribution to the Critique of Actually Existing Democracy," in Craig Calhoun, ed., *Habermas and the Public Sphere* (Cambridge: MIT Press, 1992), 109-142.

[79] Fraser, "Rethinking the Public Sphere."

[80] See e.g. Brandeis, dissenting in *New State Ice Co. v. Liebmann,* 285 U.S. 262 (1932).

[81] See e.g. *United States v. Lopez*, 514 US 549 (1995), *United States v. Morrison*, 529 US 598 (2000).

Such local authority, however, need not take the form of local autonomy immune from external influence. Rather, democratic agency can be better served by local governments with wide capacities to *initiate* policies, while remaining subject to overrule or revision by higher legislative authorities at the state or federal level. Rather than a binary debate between pure local autonomy—which magnifies concerns about irrational or illiberal local policies and chaotic 'patchworks' of social policies—and complete state authority over localities—which eliminates room for local democratic engagement and experimentation—this approach would seek to harness the democratic potential of localities while embedding them in a larger ongoing policy debate. In this view, local governments become a positive force facilitating the working out of complex social problems over time.[82] Such experimentation could be constrained by national minimum standards and basic constitutional rights, but could also give rise over time to new minimum standards and policies that can be adapted in different contexts. Cities can thus serve as important spaces for policy experimentation on everything from living wages to labor ordinances, environmental protocols, and mortgage regulations.[83]

This emphasis on facilitating local experimentation, initiative, and democratic voice suggests a broader rethinking of the ideas of federalism and decentralization themselves. Decentralization, in this approach, is less about ensuring the pure autonomy of the local, to which dissent can exit, and instead is more about multiplying the sites in which citizens, associations, and minorities can

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[82] For a similar argument see e.g. Barron, "Reclaiming Home Rule"; and Barron, "Blue State Federalism at a Crossroads," *Harvard Law and Policy Review* 3:1 (2009), 1-7.

[83] See Schragger, "The Progressive City," 39-40.

experience democratic self-government, and enact real policies. These policies in turn ought to be subject to contestation and review—but this system of initiation and review is a different one from traditional understandings of decentralization as autonomy.[84] This approach allows a democratic polity to harness the full value of democratic debate, disagreement, and dissent. Rather than limiting the capacity of alternative views to realize their visions in the name of uniformity, this approach suggests the polity is better served by enabling dissenting voices to actually enact their proposed policies, which can then be challenged or contested more broadly. Such "dissenting by deciding" blends self-governance with self-expression,[85] enabling dissenters to force majorities to engage with the merits of their proposed policies and visions, helping catalyze broader national debate.[86]

Progressives have historically shied away from this kind of broad local authority, in part out of the fear of extreme policies being proposed at the local level—a fear with foundation in the politics of race and other forms of discrimination. But moderation and social progress is often better served not be precluding self-governance, but rather by enabling dissenters to enact their proposals—and forcing them to actually govern on the basis of these ideas.[87] The

[84] See e.g., Heather Gerken, "Foreword: Federalism All the Way Down," *Harvard Law Review* 124:4 (2010), 1-71.

[85] Gerken, "Federalism All the Way Down," 64.

[86] Heather Gerken, "A New Progressive Federalism," *Democracy Journal* (Spring 2012), 37-49.

[87] Gerken, "Progressive Federalism," 46 ("As in the context of race, we often laud minority rights because they can knit political outliers into the polity. But the odd thing about a rights strategy for protecting dissent is that it pushes dissenters outside of the project of governance. They have a right to speak their mind, but only when they speak for themselves. Minority rule, by contrast, pulls dissenters into the project of governance. When dissenters wield local power, they can no longer jeer from the sideline. Instead, they have to suit up and get in the game. Minority rule thus requires dissenters to do just what the majority is accustomed to doing: deal with criticism, engage in compromise, figure out how to translate broad principles into workable policies. Abstraction and ideological purity are the luxuries enjoyed by policy-making outsiders. When dissenters have an

fear of minority repression, in other words, can be defused not by eliminating the space for local political agency, but by multiplying the opportunities for various kinds of minorities to exercise meaningful voice and agency. This in turn suggests that far from fearing the local, Progressive reformist politics ought to embrace the local more wholeheartedly, as another set of arenas in which citizens can experience democratic self-government, contest policies that may be in ascendance elsewhere, and innovate new approaches to social problems.

This approach better instantiates the value of self-government—and enables more effective macro policy learning through direct experience and wider variation across policy proposals.[88] Cities can thus serve as a crucial forum facilitating democratic empowerment, but for this vision to be achieved, the legal structure of city power must be altered. As Frug suggests, the central element is to expand the power of localities, for "power and participation are inextricable linked: a sense of powerlessness tends to produce apathy rather than participation, while the existence of power encourages those able to participate in its exercise to do so."[89]

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opportunity to govern, however, they must figure out how to pour their arguments into a narrow policy space.").

[88] Listoken, "Learning through Policy Variation" (noting that higher variance in policies enables more effective identification of optimal approaches).

[89] Frug, "City as a Legal Concept," 1070.

10 MORAL JUDGMENT AND THE COSTS OF AVOIDANCE

The presumption of technocratic and laissez-faire approaches to economic governance is that market aggregation or expert policymaking will conduce to the public good by generating socially-optimal outcomes that are free from the partiality, irrationality, and raw politics that characterize democratic debate. This turn to markets or experts works by depoliticizing economic policies, moving them out of the realm of political—and especially democratic—debate, to be instead formulated by neutral, rational systems of either market forces or expert oversight. But something important is lost in this attempt to depoliticize the development of economic policies and outcomes. As suggested in Part II above, a vibrant democratic polity requires that matters of moral and social concern be engaged openly, rather than submerged from contestation.

This chapter examines recent debates in financial regulation policy to explore these themes. After first offering a general argument that such matters of economic policy implicate moral, and not merely technical or neutral expert, judgments, the chapter examines two of the most prominent policy debates since the financial crisis: how to regulate too-big-to-fail (TBTF) financial firms, and how to address the proliferation of risky new financial instruments such as derivatives. In both cases, the prevailing policy discourse and legal regime have cast these issues as a matter of technical optimization through expert policy or market forces. The presumption is that only expert oversight can mitigate economic risks while harnessing the benefits of large financial firms and new financial instruments. But

this understanding of the issues submerges real moral questions at stake: at heart, both policy issues implicate the same moral judgment over the social value of finance. In both cases, the decision of whether or not to permit large firms or new instruments rests on a moral and political—rather than technical—judgment about what kinds of financial activity we value as a society, and what kinds of harms we are willing to tolerate. Redescribing both TBTF and financial innovation as moral rather than purely technical issues thus not only better describes the nature of these problems; it also opens up a wider variety of alternative reform approaches. So long as we see these issues as narrowly technical ones, this construction of the problem calls for a response that relies on technocratic expertise. More radical attempts to limit the size and activities of financial firms can be dismissed from a technocratic perspective as naïve, forgoing economic benefits out of an overly moralized disapproval of certain financial firms or activities. But when the issues are understood in their moral and political dimension, these policy alternatives start to look more apt.

Yet the institutional history of financial regulation has been driven by an effort to *avoid* such controversial moral questions, delegating them to expert regulators or to the market itself. This effort at moral avoidance, however, is a costly mirage. The transference of financial policy to experts does not resolve moral controversy; it only displaces it to a proxy battle over the scope of expert authority. Indeed, this effort to sterilize financial regulation of controversial moral judgments drove the very construction of technocratic financial regulatory institutions, undermining the kinds of democratizing channels of participation and decentralization outlined in pervious chapters. These debates also paradoxically

produced some of the pathologies of financial regulation that helped fuel the 2008 crisis itself.

Expertise and moral judgment in economic discourse

Despite the promise of expertise as a way to resolve social problems through apolitical rationality and knowledge, expertise is necessarily inflected with subjectivity, moral judgment, and politics. For critics within the economics discipline, this illusion of scientific mastery contributed to the proliferation of overly optimistic models of self-correcting financial markets, such as the theory of efficient financial markets which justified much of the deregulation of finance.[1] As Paul Krugman argued later, "the economics profession went astray because economists, as a group, mistook beauty, clad in impressive-looking mathematics, for truth."[2] Regulators followed suit, coming to see markets as self-correcting, regulation as presumptively costly and undesirable, while become less mindful of problems of concentrated financial capital, and increasingly risky market activities.[3] The financial crisis thus "forces us to reassess faith in our ability to reduce the complexities of the world into understandable systems, and to use algorithms based on those regularities to predict and control the future."[4] But the

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[1] See Justin Fox, *The Myth of the Rational Market: A History of Risk, Reward, and Delusion on Wall Street* (New York: Harper Business, 2011).

[2] Paul Krugman, "How Did Economists Get it So Wrong?" *New York Times Magazine*, September 6, 2009.

[3] Harry McVea, "Financial Services Regulation Under the Financial Services Authority: A Reassertion of the Market Failure Thesis?" *Cambridge Law Journal* 64:2 (July 2005), 413-448 (on the turn to deregulation in the British Financial Services Authority).

[4] Jeffrey Lipshaw, "The Epistemology of the Financial Crisis: Complexity, Causation, Law, and Judgment," *Southern California Interdisciplinary Law Journal* 19 (2010), 299-352, at 302.

failure of economics was not just its turn to abstraction over empirics; it was also the degree to which economics as a social science and a language of policy justification presented itself as neutral, uncovering optimal social policies free of the burden or complication of moral judgment. These moral dimensions, however, cannot be eliminated from economic policy questions. As a result, expertise alone cannot fulfill its aspiration of generating neutral policy solutions to public problems.

Moral judgments inflect expertise in part because of the limits of expert knowledge. Many complex systems are difficult to master through expert knowledge and analysis, and may defy definitive technical resolution because of poorly defined outcomes, probabilities, feedback loops, and sudden changes to the system in question.[5] Further, social and political concerns often outpace scientific consensus, meaning there will always be the need for political as well as technical judgments in public policy.[6]

These limitations of expert knowledge provide laissez-faire critics of the state with an argument to turn to markets as more epistemically superior modes of governance. But this solution to the epistemic limits of expertise is also unsatisfying because, while expert knowledge may be limited, the policy issues themselves are intertwined with fundamentally moral concerns that ought not to be decided by markets or experts, but rather through democratic politics. Economic policy necessarily raises moral decisions to be made about the social value of different

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[5] Douglas Kysar, *Regulating from Nowhere: Environmental Law and the Search for Objectivity* (New Haven: Yale University Press, 2010), 73-5.

[6] Harry Collins and Robert Evans, *Rethinking Expertise* (Chicago: University of Chicago Press, 2007), 6-8.

kinds of financial activity, about what types of transactions to permit, prevent, or regulate.[7]

Indeed, in many policy issues, particularly in areas like economic regulation, it is not possible to determine a neutrally 'correct' policy solution, since any such computation will necessarily rest on moral judgments about what interests and factors should be considered, how they should be valued, and weighted. As Douglas Kysar argues in context of the debate over expertise and technocracy in environmental regulation,

> The most worrying danger presented by cost-benefit analysis is not that we will choose the wrong modeling assumptions, but that the full power and responsibility of our collective agency will become lost amidst the rhetorical force of an interest-aggregation exercise that purports to take account of all relevant consequences of social choice. This semblance of comprehensiveness is misleading: the answer that cost-benefit analysis provides work a narrowing of the questions that environmental law asks.[8]

Much the same can be said in context of economic regulation. Economics as a discipline claims unique understanding of the economy and of specialized tools of statistical, mathematical, and cost-benefit analysis. But while there is real vital knowledge in the discipline that is relevant for policy disputes, it is important to remember that economics—like any social science—is also inextricably political, carrying normative implications for what we ought to do as a society. The use of mathematical models, statistical tests, and other arguments more often than not function as a form of rhetoric, as figures of speech to persuade, convince, and advocate.[9] This is not to belittle economic or social science; rather it is to

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[7] See e.g., Lipshaw, "The Epistemology of the Financial Crisis," 347-51.

[8] Kysar, *Regulating From Nowhere*, 119.

[9] See Deirdre N. McCloskey, *The Rhetoric of Economics* (Wisconsin: University of Wisconsin Press, 1998).

acknowledge that all claims to expertise—especially when in context of a policy dispute—are partly attempts at persuasive conversation aimed at shaping social action.[10]

These limits of expertise are no reason to throw up our hands.[11] Rather, they points to the need to subordinate and embed expert analysis on broader democratic debate over the moral issues at stake. If economic expertise cannot fully capture the complexity and moral dimensions of a policy matter, then far from being a source of disempowerment, this instead opens up the terrain for a broader morally-inflected discussion of what the right thing to do might be. As some scholars of expertise have noted, lay persons do possess some forms of tacit, local, and experiential knowledge that are crucial to informed policy judgment.[12] But more importantly, as democratic citizens, we all deserve a voice in the normative and political questions that help shape our social realities and possibilities. Thus,

> there is no reason to think ordinary people are any less capable of correcting their mathematical errors after dialogue with others than are technocrats. …Our task is not to refine a technocratic standard of rationality alien to people's concerns, but to empower people to speak and act for themselves.[13]

The lesson of the financial crisis is not only that our experts lack sufficient knowledge. It is that expertise alone is not enough. Our attempts to erase the

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[10] McCloskey, The Rhetoric of Economics, 162, 179.

[11] Lipshaw, for example, seems to suggest as much: "The conundrum, of course, is that if it takes an expert to see the problem caused by complexity, how are the rest of us (ordinary people as well as the intermediates) who possess merely common sense supposed to do anything but rely on their judgment?" Lipshaw, "The Epistemology of the Financial Crisis," 303.

[12] See Collins and Evans, *Rethinking Expertise*, 28-40.

[13] Elizabeth Anderson, *Value in Ethics and Economics* (Cambridge: Harvard University Press, 1993), 216.

dangers of moral judgments in economic policy through appeals expert knowledge or market forces are therefore bound to fail.[14] An over-reliance on expertise risks the displacement of moral and political agency of citizens themselves. In grappling with these limits of their knowledge, expert policymakers must necessarily engage in subjective judgments, but the rhetoric and stature of expertise is such that it seeks to efface this subjectivity, removing it from view.[15] As a result, such claims to expertise remove from the domain of political contestability matters of moral and political concern, under the guise of neutral, objective expertise that can seemingly resolve such thorny policy issues through calculation and optimization.[16] Instead, these questions must be addressed through a more openly moral debate through democratic politics—a debate in which economic expertise can offer insight, but not resolution.

Incorporating such moral and political debate would seem to be a recipe for even more controversial, ineffectual, or socially undesirable policy outcomes. But rather than trying ever harder to sterilize policy debates from the political, we must instead acknowledge the irreducibility of politics and find ways to integrate the political and the expert in productive ways. As Mark Brown argues, efforts to rid science of politics implies that scientific expertise can be free of politics and value judgments altogether, but the analysis of complex multifaceted problems necessarily entail value judgments of some kind—particularly in the case of political problems which are generally ill-formed, with tremendous uncertainty,

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[14] Lipshaw, "The Epistemology of the Financial Crisis," 304.

[15] Kysar, *Regulating From Nowhere*, 32; David Kennedy, "Challenging Expert Rule: The Politics of Global Governance," *Sydney Journal of International* Law 27 (2005), 5-28, at 11.

[16] Kennedy, "Challenging Expert Rule," 5-12; Kysar, *Regulating From Nowhere*, 67.

and no single optimal solution.[17] As a result, such efforts paradoxically turns science into more of a "proxy battleground for politics,"[18] where different sides cherry pick their experts, making experts both more necessary and powerful, and also less trusted.[19] Thus,

> efforts to eliminate politics from science advice inevitably lead to conflicts over what is 'political.' The result is to displace the political conflict onto science. Science becomes a proxy battleground for politics. In this respect, those calling for science advice free of politics are as guilty of politicizing science as their adversaries—even as they simultaneously scientize politics, by implying that political questions can be resolved by science.[20]

What is needed is an alternative way to enable inclusive deliberation and contestation in the democratic process that is informed by, but not subordinated to, the claims of expertise.[21] By acknowledging the realities of moral and political dimensions to seemingly technical issues, those issues can be opened up to a wider range of democratic contestation. While potentially tumultuous, such democratization of economic policy debates better than the total delegitimization and rejection of expert knowledge altogether.[22]

Conventional economic governance has been largely driven by an effort to sidestep and avoid this kind of moral democratic judgment about what constitutes a desirable economic order as naïve at best, dangerous at worst. The attraction of both technocratic and efficient markets approaches to this question lies in their

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[17] Mark Brown, *Science in Democracy: Expertise, Institutions, and Representation* (Cambridge: MIT Press, 2009), 2, 11.

[18] Brown, *Science in Democracy*, 3.

[19] Brown, *Science in Democracy*, 11-12.

[20] Brown, *Science in Democracy*, 3.

[21] Brown, *Science in Democracy*, 3.

[22] Kennedy, "Challenging Expert Rule," 23.

promise of offering a morally neutral way of understanding the complexities of modern financial capitalism, suggesting straightforward ways to optimize the market's functioning for social welfare. Despite the allure of neutrality and market optimization, however, this effort to sidestep the fundamentally moral questions of economic governance is misleading, and ultimately narrows our range of possibilities in response to the problems of the market economy.

These costs of moral avoidance in the allure of neutral expert management can be seen in two of the headline policy debates to emerge from the 2008 financial crash: the question of how to regulate too-big-to-fail (TBTF) firms, and the question of what to do about the innovation of new financial instruments like derivatives. The mainstream policy response to both issues has turned to experts as key to developing technical policies that mitigate the risks of TBTF firms and new financial instruments while harnessing their contributions to economic growth. While some more radical reformers argued for more structural reform approaches that institutionalized limits on the size or permitted activities of financial firms, these approaches were dismissed as naïve, imposing an overly moralized attack on the financial sector where a more neutral and expert-led approach of market optimization was necessary. But both of these policy issues at their core rest on a moral judgment about the social value of finance. Our moral stance on the social value of TBTF firms and new financial innovations is implicit in any regulatory regime. Bringing this moral question of the social value of finance to the fore provides a fuller description of the problems posed by TBTF firms and financial innovation, and in so doing provides a more solid normative foundation for more radical, structural reform possibilities.

The social value of finance

As economist Benjamin Friedman notes, the awareness of the tremendous social costs brought on by the financial sector—in terms of unemployment and economic recession following the crisis, and the risk of future crises—must be linked to the substantive role that financial markets do and ought to play in modern society. Otherwise, how can any public policy make appropriate decisions about how to regulate the sector?[23]

As Friedman argues, the basic social functions of finance are simple: the industry offers individuals a mechanism for saving, while converting these savings into socially-beneficial investment. First, and most importantly, financial markets provide a critical mechanism to channel the savings of individuals and businesses into productive investments. Through such "intermediation" banks lend out cash they receive as deposits, providing credit and capital to businesses, thereby promoting broader economic activity. Similarly, finance links longer-term flows of funds into shorter-term provisions of credit and resources. In such "maturity transformation," basic securities such as mutual funds and bonds can provide day-to-day financing for businesses and individuals out of a pool of longer-term savings. Third, finance provides credit for individuals and businesses enabling them to balance their consumption and income against fluctuations, protecting themselves against various economic risks through insurance or certain forms of hedging. Finally, all of these practices can help promote economic activity directly by creating employment within the financial sector, and indirectly by supporting the ability of other firms and businesses to thrive.

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[23] See Benjamin Friedman, "Is Our Financial System Serving Us Well?" *Daedalus* (2010), 9-21.

These basic functions must be weighed against the full range of social costs of the financial sector as currently constituted: not only the risk of future financial crises, but also the costs arising from bubbles where financial firms misallocate investment into sectors such as housing in the 2000s and the telecom bubble of the 1990s; opportunity costs as financial firms came to represent a highly disproportionate share of all corporate profits and wages paid in the American economy; and social costs as financial firms came to absorb a disproportionate proportion of highly skilled and educated workers.[24] Any additional benefits from the financial sector—in particular, the profits and wages derived from trading in more complex financial instruments such as derivatives—may benefit the individuals involved in those transactions, but provides little value to society as a whole. These are precisely the financial activities that magnified the risks of a financial crisis, in which financial regulation can try to limit.

The mainstream accounting the social contribution of finance generally sums the output of the financial sector, which in the US in 2010 combined for $1.2 trillion, or 8 percent of GDP.[25] But as Andrew Haldane, chief of financial stability at the Bank of England, has argued, this kind of accounting of the social value of finance does not distinguish between greater *risk-taking* which may not necessarily raise social welfare, and *risk-management*, which is the core of the social value of finance. Adjusting for this distinction reduces the estimated value-added of the

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[24] Friedman, "Is Our Financial System Serving Us Well?", 13-16. See also Paul Kedrosky and Dane Stangler, "Financialization and Its Entrepreneurial Consequences," Kauffman Foundation Research Series, March 2011 (finding that human capital increasingly flowed into the financial sector during the 1990s and 2000s, creating a feedback cycle as finance came to displace productivity, innovation, entrepreneurship, and job growth in other parts of the economy).

[25] Andrew Haldane, "What is the Contribution of the Financial Sector?" *VoxEU*, Nov 22, 2011.

financial sector significantly.[26] And this does not count the social costs from financial crises—and the implicit subsidies for too-big-to-fail firms that Haldane estimates to be as high as $1 trillion from 2007-2010—several times the annual profitability of the largest global banks in the five years prior to the crisis.[27]

This assessment of the actual social value of finance suggests two things. First, a line can be drawn between socially desirable and socially harmful financial transactions. Second, that regulations that limit the latter may be desirable even if they cut into the wealth and value of the financial sector itself. By putting the question of the social value of finance at the center of the regulatory question, we can motivate regulatory approaches that rely not on sporadic technocratic oversight or minimalist regulation, but instead on structural changes that can help prevent social harms by limiting in various ways the activities of the financial sector: "starting from the view of the financial sector as a servant of the broader economy and society, rather than as a master, would produce a radically different approach to its regulation."[28]

The limitations of bypassing this kind of moral judgment by appeal to expertise, can be seen in two distinct policy areas: the debate over regulating the size of TBTF firms, and the debate over regulating the innovation of new financial instruments like derivatives. In both of these areas, the mainstream policy response turned to expert oversight as a way to avoid these controversial moral judgments over the value of different kinds of financial activity, relying on experts

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[26] Haldane, "What is the Contribution of the Financial Sector?"

[27] Haldane, "What is the Contribution of the Financial Sector?"

[28] John Quiggen, "Financial Markets: Masters or Servants?" *Politics and Society* 39:3 (2011), 331-46.

to mitigate economic harms without legislating away entire firms or activities. By contrast, engaging with this question of the social value of finance opens up a wider array of reform possibilities that impose more stringent limits on financial firms and activities. Regardless of which of these policies are ultimately pursued, what they share is a willingness to impose a more stringent constraint on financial firms and transactions, rooted in an underlying moralized judgment about the social value of those firms and transactions.

Too-big-to-fail as a moral category

One of the major policy issues since the financial crisis has been over how to identify and regulate "systemically risky" or TBTF financial firms—firms whose collapse would threaten the entire financial system as Lehman Brothers did in 2008. Dodd-Frank's approach to this problem of TBTF firms is essentially to defer to expert oversight. The statute creates a Financial Stability Oversight Council (FSOC) comprised of the heads of the major financial regulatory bodies, chaired by the head of the Federal Reserve Bank, tasked with first identifying and then regulating appropriately TBTF firms. On the surface, TBTF regulation seems a quintessential domain for such technical expertise. How else are we to determine when a firm becomes sufficiently large and interconnected that they pose a systemic risk to the financial system? How else would we calibrate regulations on these firms to ensure the continue to contribute to the macroeconomy while mitigating the potential of a catastrophic collapse? Dodd-Frank thus seeks an apolitical approach to the problem of TBTF firms.

But expertise alone cannot fully address the problem. Experts themselves disagree on the causes and responses to TBTF. Existing efforts by policymakers

and economic academics to define the category of TBTF firms and systemic risk are surprisingly slippery, using a range of metrics but without any clear consensus.[29] The problem is that "systemic risk" and "too-big-to-fail" are not technical economic concepts, but rather political judgments. Labeling a firm as TBTF, or as posing systemic risk, is another way of saying that we as a society are unwilling to bear the social costs of their collapse.[30] TBTF firms might be "large" in terms of assets, interconnectedness, or even in terms of their implications for the labor market.[31] The slipperiness of the concept of TBTF stems from the moral nature of this identification of the social harms that warrant resolution by the state. The problem is analogous to what Brandeis faced with public utilities in *New State Ice*, discussed in Chapter 7 above: when a private firm implicates a vital social necessity, it may warrant more severe political scrutiny and oversight, but this determination is ultimately a political, not a technical one.

Indeed, so long as TBTF and systemic risk are understood as issues of purely technical complexity, the turn to expert oversight may seem reasonable. As a technical matter, the challenge of mitigating the risks of TBTF firms while harnessing their economic potential seems to require fine-tuned calibrated regulations developed through expertise. But if TBTF and systemic risk are moral categories, then these determinations cannot be made purely on the basis of expertise. Recognizing this policy domain as a fundamentally moral judgment unlocks a wider array of reform avenues. Instead of relying on expert oversight,

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[29] See Adam Levitin, "In Defense of Bailouts," *Georgetown Law Journal* 99 (2011), 435-514, at 445.

[30] Levitin, "In Defense of Bailouts."

[31] Levitin, "In Defense of Bailouts," 451-55.

TBTF as a moral problem can also be addressed through more structural reforms that limit the size and powers of TBTF firms thus eliminating the problem of systemic risk. This more structural approach, while dismissed as naïve or economically harmful, relies on a moral judgment about what kinds of financial activities and firms we value as a society.

Historically, the idea of fundamentally restructuring corporations as a way to limit their harmful effects has been a staple of reform politics, especially in the antitrust movements of the late nineteenth and early twentieth centuries. These views gradually went out of favor over the course of the New Deal, as noted earlier. But they continue to provide a compelling avenue for realizing a more democratic political economy in which the dangers of concentrated private power and harmful economic repercussions of various industries can be curtailed. As noted in Chapter 2, Dodd-Frank approached the TBTF problem through an appeal to expert oversight. But a rival camp of reformers called for a return to traditional Progressive principles of antitrust. For these advocates, the problem of TBTF was simple: like the railroad and oil trusts of the early twentieth century, these firms had acquired control over too great a share of the nation's financial system, and thus should be broken up into smaller entities. These smaller entities would then pose no real threat to the broader financial system if they engaged in abusive practices or failed entirely. [32]

Whether using the Brown-Kaufmann standard of capping the total deposits of financial firms at some percentage of GDP, or by using the Federal Deposit

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[32] Simon Johnson, "White House Should Also Announce An Antitrust Investigation into Major Banks," *Baseline Scenario*, January 21, 2010; Krishna Guha, "Opening salvo on banks has yet to come," *Financial Times*, January 18, 2010.

Insurance Corporation's already-existing metrics of firm size,[33] an antitrust approach is feasible. Further, it resolves the problems that continue to plague the technocratic approach of Dodd-Frank: by creating a bright-line rule, an antitrust approach forces firms to choose between maintaining a certain size or being broken up by the government, preventing the moral hazard of bailouts, and the difficulties regulators face in credibly and effectively implementing complex regulation without succumbing to risks of capture.[34]

Economist Nouriel Roubini furthered this position, arguing in *Newsweek* that large TBTF banks were not only too big to fail, but were also "too big to exist, and too complex to be managed properly."[35] For Roubini, the anxieties about reducing financial sector profits and innovation were misleading; these claims to efficiencies and social benefits from complex financial securities were over blown. "The TBTF firms consider themselves essential to the world economy," Roubini argued. "Thanks to their scale, we're told, they offer "synergies" and "efficiencies" and other benefits. The global economy can't function without them, they say. This is preposterous." In reality, these activities were little more than risky profit-making bets, which created bubbles rather than adding real social value to the broader economy. The entire purpose of tougher regulations, then, is and ought to be the reduction of corporate profits which would induce the reorganization of these firms along less risky lines. Roubini ultimately called for even more aggressive bright-line limits on what financial firms

[33] Jonathan Macey, James Holdcroft, Jr., "Failure Is an Option: An Ersatz-Antitrust Approach to Financial Regulation," *Yale Law Journal* 120 (2011), 1368-1418, at 1371-3.

[34] See Macey and Holdcroft, Jr., "Failure Is an Option," at 1372-3; 1382-3.

[35] Nouriel Roubini, "Bust Up the Banks," *Newsweek Magazine*, May 6, 2010.

could do: not only restoring the Glass-Steagall separation of investment and commercial banking and implementing the Volcker rule ban on proprietary trading, but also banning investment banks from doing any short-term borrowing in the first place, thus reducing the chain reactions caused by the collapse of firms like Lehman Brothers.

These proposals were largely marginalized in the reform debate around Dodd-Frank itself. But if instead we were willing to address this question of the social value of finance and impose structural limitations on financial firms in the name of the public good, the old antitrust vision suddenly becomes more viable and current. The problem preventing an antitrust approach is one of ideas and vision, not one of technical capacity or administrability.

"Speculation" and financial innovation

A second key policy debate since the financial crisis concerns how to regulate new financial instruments like derivatives and futures contracts that helped create the kind of complex mortgage-backed securities that gave rise to the crisis. Indeed, throughout the debate over the 2008 financial crisis, one of the key disputes was over what large financial firms that engaged in complex derivatives and mortgage- backed securities trading actually *did*. Many of these firms defended their innovation and se of complex financial instruments as a form of "market-making," creating new mechanisms to channel funds into economic investments thus promoting economic productivity. Critics meanwhile argued that these instruments were simply a way for these firms to speculate, creating huge profits for themselves and large risks for the taxpayer. As one bank executive complained to the *New York Times*, modern finance "has become a virtual

casino."[36] As with the case of TBTF regulation, this debate has largely been pursued by relying on expert judgment of regulators in the Federal Reserve Board, the Securities and Exchange Commission (SEC), the Commodity Futures Trading Commission (CFTC), and elsewhere to oversee the use of these financial instruments, mitigating their risks, while harnessing their economic benefits. But derivatives and futures regulation is fundamentally a moral question about what kinds of financial activities we as a society sanction—as "productive" work—and what kinds we disapprove of as "speculation."

As Simon Johnson and James Kwak, two of the most vocal critics of the financial sector during the crisis, noted, "today's challenge is to rethink financial innovation and learn how to separate the good from the bad."[37] If the main purpose of finance is to channel savings into investment, and to link long-term savings to the shorter-term funding needs of companies seeking credit and loans, then financial innovation is good only when it improves this task of financial intermediation *in socially productive ways*. The development of new securitization techniques like credit default swamps and collateralized debt obligations did improve financial intermediation, creating a new species of mortgage-backed securities that were so seemingly safe that even pension funds and money market mutual funds would buy them. But such financial innovation is ultimately detrimental, for it essentially manufactured safe-looking assets out of fundamentally unsound subprime mortgages.[38]

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[36] Joe Nocera, "The Good Banker," *New York Times*, May 30, 2011.

[37] Simon Johnson and James Kwak, "Finance: Before the Next Meltdown," *Democracy: A Journal of Ideas* (2009), 19-24, at 20.

[38] Johnson and Kwak, "Finance: Before the Next Meltdown," 21-22.

Instead of giving the financial sector a free hand to "innovate" subject only to some loose risk constraints, regulation should emphasize consumer protections to prevent individuals from falling subject to predatory lending and usury; standardized terms for securities to prevent the spread of 'toxic' assets into areas such as pension and mutual funds seeking to maintain stability; and spreading financial services to the unbanked and businesses in need of credit.[39] As Johnson and Kwak argue,

> The role of financial regulation should be to discourage innovation that produces excessive intermediation and promote innovation that delivers financial services that people need. The key to any successful regulatory regime is therefore discerning the difference between good and bad financial innovation. Right now, ours doesn't. … [Current reforms] follows the old conventional wisdom—that innovation is inherently good, and regulators need only watch out for abnormal excesses or "bad apples." Instead, the presumption should be that innovation in financial products is costly—it increases transaction costs, the cost of effective oversight, and the risk of unanticipated consequences—and should have to justify itself against those costs.[40]

Put another way, innovations that protect or expand the social benefits of finance—such as through more effective linking of savings and investment, expansion of basic credit to the unbanked, and job creation through investment in new businesses—are of a different normative and social value from the kinds of financial innovations that marked the boom in the financial sector in the years leading up to the financial crisis. While the explosion of exotic new securitization practices generated windfall profits for relatively few workers in the financial sector, they did so in ways that not only created risks of systemic financial collapse, but also in ways which concentrated greater social resources in the

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[39] Johnson and Kwak, "Finance: Before the Next Meltdown," 23-24.

[40] Johnson and Kwak, "Finance: Before the Next Meltdown," 22-23.

relatively small number of persons involved in the financial sector, widening inequality and supplanting activity in the real economy.[41] Further, such negative innovation creates unjustifiable risks for the broader polity to enrich the few in the financial industry.

A willingness to cut into financial profits to distinguish socially valuable transactions would open up a variety of more stringent regulatory approaches to financial instruments like derivatives and futures contracts. First, and most simply, all complex financial transactions like derivatives, futures, and swaps could be subjected to a financial transactions tax which would impose an additional cost on financial firms and traders. This would decrease the frequency and volume of transactions perhaps enough to reorient financial activity towards safer channels.

Second, futures contracts, like the over-the-counter (OTC) derivatives that played such a large role in magnifying the risks and costs of the mortgage-backed securities collapse, could be limited by a government regulator akin to the Food and Drug Administration, with the power to approve transaction types as safe, or acceptable after weighing the social costs and benefits. While many products can be used to either hedge or speculate, some products such as the credit default swaps and collateralized debt obligations at the heart of the mortgage-backed securities collapse arguably have no non-speculative value. An agency could identify socially beneficial financial products as those whose welfare gains from insurance outweigh the likely costs from speculation, permitting only those

[41] See e.g. Greta Krippner, *Capitalizing on Crisis: The Political Origins of the Rise of Finance* (Cambridge: Harvard University Press, 2011).

transactions that pass this test.[42] This proposal is interesting because while it retains a faith in technocratic expertise, it nevertheless pushes farther than Dodd-Frank because it engages directly with the effort to distinguish socially desirable from undesirable financial activities, and is willing to accept a hit to the profitability and wealth of the financial sector in exchange for a more stable economic order.

A third, and even more compelling, approach to regulating derivatives would go one step further, addressing the moral distinction between speculation and risk-mitigation in a way that does not necessarily rely on the capacities of expert government regulators. To the extent that Dodd-Frank reverses the deregulation of derivatives from, it remains reliant on the CFTC to draft or loosen the requirements for derivatives trading.[43] This conventional appeal to expertise seems alluring because it delegates controversial judgments over productive versus speculative transactions to expert regulators. By contrast, a more explicitly moralized approach could simply make futures contracts legal but unenforceable, thus limiting speculation by making traders internalize the full costs of their gambles without relying on the government as an overseer or gatekeeper to financial markets. In effect, this approach flips the laissez-faire critique on its head: it is now proponents of market exchanges like futures contracts, rather than the state, who must bear the burden of enforcing—and therefore justifying the broader social value of—these transactions. The goal of distinguishing productive

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[42] Eric Posner, E. Glen Weyl, "A Proposal for Limiting Speculation on Derivatives: An FDA for Financial Innovation," Working paper, on file, January 26, 2012.

[43] Lynn Stout, "Derivatives and the Legal Origin of the 2008 Crisis," *Harvard Business Law Review* 1 (2011), 1-38, at 31-4.

from speculative finance is thus achieved without the dangers of capture, ineffectiveness, and lack of knowledge that plague technocratic solutions to the problem of modern finance.[44]

Traditionally, common law required speculators who wager on prices through futures and options to make and accept the deliver of the goods and services being traded. This stance persists in modern law through legal rules on insurance—where a party can only collect insurance on something where they have a demonstrable interest—and through the Commodities Exchange Act (CEA) which had required that futures contracts that were *not* being collected or delivered were only permitted on regulated exchanges, where traders and reputation costs could limit excessive speculation. The CEA thus codified the common law rule, forcing traders to cabin speculative activities on regulated exchanges that imposed technical limits on issues such as margins, positions, and short-selling—restrictions weakened by the deregulatory push in the 1980s.[45] This tradition of legal limits on speculation continued to animate the 1934 Securities and Exchange Act. In securities markets, where there are no physical goods to be delivered, the problem of speculation is even more rampant, and the debate around the 1934 Act explicitly revolved around this need to prevent speculation as a moral and economic harm.[46]

The broader ascent of economic understandings of efficient financial markets viewed speculation as ultimately productive, abandoning anti-speculative

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[44] Lynn Stout, "Why the Law Hates Speculators: Regulation and Private Ordering in the Market for OTC Derivatives," *Duke Law Journal* 48 (1999), 701-86.

[45] Stout, "Speculators," 713.

[46] Stout "Speculators," 727-31

language as anachronistic.[47] But the historical unease with speculation was not anachronistic nor irrational; rather it reflected a very real moral and economic sensibility that sought to discourage unnecessary increases in risk and wastage of human and financial capital on socially unproductive activities.[48] Dodd-Frank did not really recapture this earlier tradition of financial regulation, but a more aggressive constraint on derivatives and speculation could do so.

Regulating financial firms as public utilities

If the social value of finance is limited to providing safe vehicles for saving and linking savings to investment, then this suggests another, even more aggressive form of regulatory oversight of financial firms as a *public utilities*. In this approach, financial firms would be tightly regulated in the same way that electrical or water utilities are to ensure they provide the basic social services safely. Other forms of financial activity would either be disallowed, or separated entirely from the most critical functions served by these firms.

This approach of regulating social necessities as public utilities has a long tradition; as noted in Chapter 3, Progressive Era reformers established utilities in a range of socially-important industries including water, electricity, gas, telecommunications, banking, insurance, and transportation.[49] To treat these industries as public utilities was not necessarily to require public ownership and

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[47] See Stout "Speculators," 735-40; See also Fox, *Myth of the Rational Market*.

[48] Stout, "Derivatives," at 11-13.

[49] William Novak, "Law and the Social Control of American Capitalism," *Emory Law Journal* 60 (2010), 377- 405, at 400.

administration of the industries; but it did articulate a deep public concern with the functioning of these agencies, opening up a much wider range of regulations as part of the effort to ensure social control of the industries to ensure the common good. Brandeis, a vocal proponent of the Progressive use of public utilities, explained that when "the public's concern about a particular business may be so pervasive and varied as to require constant detailed supervision and a very high degree of regulation," private industries may be treated as "public" because they affected the public interest so significantly.[50] Regulation would thus be used to provide a vital social function in a collective, cooperative manner, directing activities in socially desirable channels, expanding the benefits of finance, and protecting a core industry that serves as a backbone or basic utility for much of the rest of the economy.[51]

For example, the New Deal era Public Utility Holding Company Act (PUHCA) subjected public utilities such as electrical utilities to extensive state regulatory oversight for much of the twentieth century.[52] Under PUHCA, utilities were required to register with the SEC, which would then scrutinize the utilities,

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[50] *New State Ice Co v. Liebmann*, 285 US 262, at 301 (Brandeis dissenting).

[51] See e.g. Joseph Heath, "The Benefits of Cooperation," *Philosophy and Public Affairs* 34:4 (2006), 313-351, making a similar argument about reconceiving the welfare state as a constructive realization of a socially desirable form of cooperation, rather than as merely a residual response to the market economy.

[52] PUHCA was passed in 1935, and empowered the SEC to dismantle and simplify the corporate structures of utilities. This power lay dormant until the 1940s and 1950s, when it was employed as a tool to respond to the growing concentration of corporate ownership of local electrical utilities. PUHCA shared a similar motivation as antitrust reforms, but instead of breaking up firms through lengthy litigation which often would not favor the government's antitrust effort, it employed regulatory agencies to restructure the firm in question, defusing concerns about conflicts of interest, and excessive pricing for consumers, while also ensuring fair voting shares for security holders in the utility. See Roberta Karmel, "Is the Public Utility Holding Company Act a Model for Breaking Up the Banks That Are Too-Big-to-Fail?" *Hastings Law Journal* 62 (2011), 821-864, at 827-8, 846-56.

assessing their corporate structures and business practices to prevent internal conflicts of interest, unfair prices and terms for consumer, and other similarly abusive activities. The experience of PUHCA could be applied to banks, preventing the problems of TBTF without resorting to costly antitrust litigation, which historically has favored Wall Street over the federal government.[53]

The public utility framework ports easily to the financial sector. The modern financial system is effectively a public-private partnership that provides a critical resource upon which all depend: the basic money supply itself. The government insures and regulates the money supply through deposit insurance and other regulations aimed at preventing runs or crashes, while banks engage in the business of making investment allocation decisions.[54] The utility framework suggests that so long as firms provide basic money supply functions, they should be tightly constrained to focus on this basic function, insulated from risky bets or toxic assets that would compromise this core economic foundation. Arguably, at its height, the package of New Deal banking regulations achieved a utility-like regulatory regime where "postwar commercial banking became similar to a regulated utility, enjoying moderate profits with little risk and low competition."[55] This system of "boring banking"—a system that lacked the complex array of wildly profitable and risky securities that marked the pre-2008 crisis economy—

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[53] Karmel, "Public Utility Holding Company Act," 843-4.

[54] See Morgan Ricks, "Regulating Money Creation After the Crisis," 1 *Harvard Business Law Review* 75., at 120.

[55] Simon Johnson and James Kwak, *13 Bankers: The Wall Street Takeover and the Next Financial Meltdown* (New York: Vintage, 2011), 35.

proved more than adequate to facilitate postwar economic growth and relatively high incomes for workers in the financial sector.[56]

This utility approach would imply a segmenting the financial sector into two distinct domains. The first domain would be that of narrow banking, where firms would focus exclusively on essential financial services—taking deposits, providing savings vehicles, and extending basic credit loans. The second domain would consist of more complex, profitable, and risky firms that focus on more exotic financial activities such as securitization and other forms of investment banking. The narrower domain of banking would then be tightly regulated to ensure the basic provision of those financial services carries on without interruption or contamination by excessive risk-taking and complex potentially toxic securities. The other domain of financial activity could then be safely left alone to engage in profit-maximizing activities, since the core social function of depositories, savings, and basic credit had been cordoned off and insulated from the potential risks of these more risky activities.[57] The basic functions of narrow banking can in fact be successfully pursued without the kinds of complex securitization and brokering activities of more complex financial firms such as investment banks. Consumer needs such as checking accounts and vehicles for savings can be easily provided by simple banks or even by publicly-run mechanisms.[58]

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[56] Johnson and Kwak, *13 Bankers*, 61-4.

[57] See John Kay, "Should We Have Narrow Banking?" *The Future of Finance*, London School of Economics Report, 2010, 217-234.

[58] See Friedman, "Is Our Financial System Serving Us Well?", 10.

Thus, this utility framework would also suggest that such constraints extend to all firms that provide money-creation services even if they are not currently regulated as depositories. Thus, part of the problem of the 2008 crisis arose from the proliferation of "shadow banks," firms that were not cash depositories and thus existed outside the tight regulations on those firms, but nevertheless held cash-like deposits such as repo agreements and money market mutual fund shares. Part of the 2008 collapse came from a run on these money-like instruments stored in this shadow banks—a danger made possible precisely because these firms were permitted to engage in money supply functions outside of the regulatory regime that ordinarily applies to traditional banking.[59]

Nor is the idea of banking as a public utility unprecedented. States or the federal government could easily provide basic banking services for deposits with clear fee structures, following the leads of states like North Dakota and Montana, creating a "public option" for banking that would not only offer secure depositories but also provide a lever for investing in new industries and competition for private firms to offer similarly stable banking systems.[60] Indeed, in North Dakota, the official state bank provides student, residential, and private loans, operating mostly like a normal depository subject to external audits and whose profits are turned over to the state treasury. Other states including Hawaii, Washington, Illinois, Massachusetts, and Virginia have considered similar state-

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[59] See e.g. Ricks, "Regulating Money Creation After the Crisis"; Perry Mehrling, *The New Lombard Street: How the Fed Became the Dealer of Last Resort* (Princeton: Princeton University Press, 2010).

[60] Ellen Brown, "The Public Option in Banking: How We Can Beat Wall Street At Its Own Game," *Huffington Post*, August 5, 2009; Matthew Yglesias, "The Case for a Public Option for Small-Scale Savings," *ThinkProgress*; Brent Budowsky, "Time for a Public Option Bank," *The Hill*, December 8, 2009.

backed depository institutions.[61] City governments could even get in the act, creating public banking entities that function like utilities, providing basic depository and investment channeling functions under the purview of the city government.[62]

These various approaches to financial regulation—capping the size of TBTF firms, greater restrictions on derivatives, and regulating finance as a public utility—share a common feature. In each of these areas, these more stringent regulations have been avoided out of a preference for expert oversight, which appears less controversial, and offers the illusion of rational, neutral, and efficient market management. Yet all of these policy questions rest on an implicit moral judgment about the social value of different kinds of firms and transactions. A willingness to regulate on the basis of such moral approbation or disapproval opens up these more stringent reform ideas that, while expressed since the 2008 collapse, did not gain traction precisely because they were seen as *too* moralized, and thus unrealistic, naïve, or irrational. The purpose of the above discussion is not necessarily to argue for any one of these particular regulatory approaches, but rather to highlight how an engagement with—rather than avoidance of—these kinds of moral judgments opens up a much wider set of reform possibilities.

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[61] Jake Grovum, "The Bank of North Dakota: Banking's 'Public Option'" *Stateline*, The Pew Center on States, April 14, 2010 (http://www.pewstates.org/projects/stateline/headlines/the-bank-of-north-dakota-bankings-public-option-85899374841) (last accessed June 30, 2012).

[62] See Gerald Frug, "City as a Legal Concept" *Harvard Law Review* 93 (1980), 1057-1154, at 1150-1.

The costs of avoidance and the construction of technocracy

Financial regulation policy disputes, as other economic policy areas, thus implicate moral judgments about what kind of economic order we desire. Yet much of the recent history of financial regulation is animated by an effort to avoid such controversial moral judgments by transferring financial regulation policy to neutral experts or self-optimizing markets. This moral avoidance not only narrows the menu of policy options as discussed above. It also drives us to build flawed institutions of economic governance. Thus, delegating these morally-charged policy issues to regulatory experts has displaced, rather than resolved, the moral controversies over what kind of economy we desire. The result has been a transmutation of this substantive moral concern into a set of proxy debates over the scope and jurisdiction of expert regulatory authority. These proxy battles have in turn created many of the pathologies of financial regulation that helped fuel the 2008 crisis—as well as constraining the opportunities for a more democratic alternative approach to economic policy through regulatory agencies or city governments.

From moral to technocratic judgment

In 1868 the Chicago Board of Trade (CBOT) suddenly found itself in an unanticipated dilemma: investors betting on the agricultural futures market had cornered the market on grain. In an institution that had emerged as a mode for commodities dealers to protect themselves against risks such as low crop yields, such profiteering speculation hijacking a legitimate and socially-productive form of

risk hedging was troubling.[63] In traditional common law, speculative contracts are unenforceable as contrary to public policy. Similarly in popular discourse there is a long tradition of rhetoric against speculation and gambling in the financial sector. But the difficulties of distinguishing appropriate risk-mitigation from speculation or gambling gradually induced common law regulation through courts to pull back, and accept modern financial markets.[64]

In 1905, the Supreme Court ratified the emergence of futures markets like CBOT as legitimate financial transactions, withdrawing from the earlier efforts of common law to distinguish acceptable from prohibited speculative financial transactions. In his majority opinion, Justice Oliver Wendell Holmes noted that in the modern economy, many contracts are made where the buyer is not intending to take actual delivery of the goods in question. This practice, for Holmes, had to be accepted as a legitimate economic activity of hedging against perceived future risks:

> Speculation of this kind by competent men is the self-adjustment of society to the probable. Its value in well known as a means of avoiding or mitigating catastrophes, equalizing prices, and providing for periods of want.[65]

To the extent that such risk-mitigation financial transactions were problematic, for Holmes, it was only because “the success of the strong induces imitation by the weak, and that incompetent persons bring themselves to ruin by undertaking to speculate in their turn.”[66] The fact that such trades were taking

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[63] See William Cronon, *Nature’s Metropolis: Chicago and the Great West* (New York: WW Norton & Company, 1991).

[64] Roy Kreitner, *Calculating Promises: The Emergence of Modern American Contract Doctrine* (Stanford: Stanford University Press 2007), 97-99.

[65] *Board of Trade of Chicago v. Christie Grain and Stock Co.*, 198 U.S. 236 (1905) (J. Holmes, majority opinion), 248.

[66] *Christie,* 198 US, at 248.

place on a public exchange with publicly-advertised prices and the close interest on the part of businesses and individuals was evidence enough for Holmes that commodity futures trading spoke to some general public interest, and was not mere gambling.[67] Therefore, the danger of financial losses by 'incompetent' traders was simply a cost that modern society had to bear in exchange for enabling risk-mitigation strategies. Such "natural evolutions of a complex society," argued Holmes, "are to be touched only with a very cautious hand." Legislators and judges had to recognize that blanket prohibitions on such transactions were "coarse attempts at a remedy for the waste incident to every social function," and ultimately "harmful and vain.[68]

For judges like Holmes, the difficulty of distinguishing between legitimate risk-mitigation and socially-desirable channeling of resources, and illegitimate speculation seemed an empty formalism: speculative transactions had the same features and looked the same as "legitimate" productive transactions. The distinction between the two seemed to be more a matter of intention and context, too murky for courts to adjudicate. To the extent that finance still required oversight, these difficulties seemed to suggest the need for neutral, technocratic expertise capable of identifying the public good in ways that retained the social benefits of finance. Combined with the attractiveness of the broadly acceptable, neutral pursuit of economic growth via greater financialization of the economy, this turn to expert management helped erode the rich moral discourse that animated earlier generations of financial reformers.

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[67] *Christie,* 198 US, at 249.

[68] *Christie,* 198 US, at 248-9.

By the New Deal era, the historical aversion of common law to speculative finance had been supplanted by the emergence of the modern regulatory state. Financial transactions were now a problem for the regulatory state, not common law. This shift to expertise helped move the policy discourse further away from a strong moral engagement with the debate over productive versus speculative uses of finance. So long as expert regulators were on the case, it seemed less vital to manage difficult distinctions between productive and speculative finance. In one emblematic case, an Illinois court rejected a suit alleging futures contracts were invalid gambling transactions, arguing that with the advent of modern securities legislation passed by Congress and the creation of the SEC, the "various acts of Congress make it clear that our public policy now recognizes the desirability and necessity of maintaining open markets, even if they sometimes be used for gambling, in order to stabilize values in commodities and securities."[69] The old anxieties of common law about distinguishing productive from speculative financial transactions had given way to an acceptance on the desirability of modern finance, and a reliance on the technocratic oversight of the new regulatory apparatus. The problem of the social desirability of finance had thus been settled, and the thorny line-drawing problem sidestepped: "The public policy has been declared to be that these contracts for future delivery are necessary to the commerce of the people of the United States in their domestic interstate economy, and since no one can tell with what intent they are entered into, it is impossible to pick and choose among them."[70] As a result, futures contracts like those which

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[69] *Albers v. Lamson*, 42 NE.2d 627 (Ill 1942), at 630. See also Kreitner, *Calculating Promises*.

[70] *Ibid*.

troubled CBOT and Holmes, were largely accepted by the 1940s as vital to the modern economy.

Displacing the moral into the jurisdictional

But as Roy Kreitner argues, to the extent that the anxieties about potentially undesirable financial transactions persisted, they manifested in a transmuted form, as a proxy debate over the scope of expert regulatory authority.[71] While these concerns about limiting agency authority appropriately are certainly valid, many of these disputes were animated not by such jurisdictional questions, but rather by substantive disagreements over the social value of finance. By displacing the substantive question into the domain of expertise, modern financial regulation law did not resolve the moral question of the social value of finance; rather it transmuted it into an even more problematic register, resulting in policy decisions that ironically created even more pathologies in the financial regulation architecture. This pattern can be seen in two areas: disputes between courts and agencies over agency regulatory authority in finance; and disputes between federal agencies on the one hand and state or local regulators on the other.

<u>Courts versus agencies</u>

Thus, as federal banking regulation after the New Deal became primarily an exercise of federal regulatory agencies, this jurisdictional question of the reach of

[71] Kreitner, *Calculating Promises*, 158 ("Conflict over what was gambling and what was allocation of risk was handled, and settled, not according to an analytical formula that successfully distinguished between them, but rather through a more complex and less decisive cultural negotiation and displacement of the question").

agency authority became a proxy battleground for competing substantive concerns over developments in finance. For example, in the famous *Chenery* case,[72] the Supreme Court initially rejected the SEC's reorganization plan for a public utility, but upheld the exact same plan once the agency resubmitted it with additional documentation justifying the plan on the basis of the agency's expertise, deferring to this "accumulated experience" and expertise of SEC.[73] Yet the dissent saw this deference as reducing judicial review to a "hopeless formality," putting agency actions beyond the reach of the law.[74] For the dissent, what was at stake was not just the ability of courts to limit agency authority; it was also a substantive concern over what the dissenters saw as a literal taking of property, in the form of the SEC's reorganization plan that invalidated the value of the plaintiff's stock in the company.[75]

In another 1963 example,[76] the Court overruled the Office of the Comptroller of the Currency's (OCC's) approval of a bank merger, claiming the merger violated antitrust statutes. The dispute between Justice Brennan's majority opinion and Justice Harlan's dissent concerns rival interpretations of whether recent Congressional legislation implied an exemption for banks from antitrust provisions; Brennan thought they did not,[77] while Harlan thought they did.[78] This

[72] *SEC v. Chenery Corp*, 332 US 194 (1947) [*Chenery II*].

[73] *Chenery II*, 332 US, at 209.

[74] *Chenery II*, 332 US, at 210.

[75] *Chenery II*, 332 US, at 216-18

[76] *US v. Philadelphia National Bank*, 374 U.S. 321 (1963).

[77] *Philadelphia,* 374 US, at 339-54.

[78] *Philadelphia,* 374 US, at 376-96 (J. Harlan, dissenting).

dispute over the scope of the OCC's authority as a regulatory agency and implicit Congressional intent, however, operated as a proxy battle for a deeper disagreement between Brennan and Harlan over the growing concentration in the banking sector and the role of banking and finance in modern society. Brennan's opinion emphasizes the "definite trend towards concentration" in the banking sector,[79] noting that the proposed merger would result in an entity that accounted for over one-third of the region's total deposits, assets, and net loans.[80] For Brennan, this level of concentration poses a clear threat to the public good, which cannot be overcome by the banks' or the OCC's claim of the economic development from the proposed merger.[81] Brennan operates on a presumption against financial bigness, noting that the critical nature of banking for the economy makes anticompetitive concerns more, rather than less, important.[82] By contrast, Harlan emphasizes the expertise of the OCC and regulatory agencies, suggesting that agencies rather than courts are the better arbiters of the public good here, and noting that the centrality of banking and finance to broader economic activity warrants looser and more flexible regulatory constraints.

As the financial sector was gradually deregulated after the 1980s, these proxy debates over agency authority paradoxically helped create some of the regulatory gaps and pathologies that gave rise to the eventual boom and 2008 crash, out of an effort to sidestep those same substantive controversies. In 1983,

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[79] *Philadelphia,* 374 US, at 325.

[80] *Philadelphia,* 374 US, at 331.

[81] *Philadelphia,* 374 US, at 364-71.

[82] *Philadelphia,* 374 US, at 371-72.

for example, OCC loosened its prohibitions to now enable retail banks to provide brokerage services.[83] As a result, banks rushed into this profitable new industry, but operated free of the regulations that the SEC had traditionally imposed on non-bank brokerages. To remedy this regulatory gap, the SEC moved to extend those regulations to these retail banks entering the brokerage industry. The DC Circuit court, however, struck down the SEC's move on the grounds that the SEC rule reached beyond its Congressional authorization: the Securities Exchange Act provided strict and clear definitions of broker, dealer, and bank, and the SEC did not have authority over statutorily-defined banks.[84] Yet this argument is perverse; as the SEC pointed out it its defense, the Congressional allocation of regulatory authority between the SEC and other agencies was premised on a background assumption that banks were already precluded from brokering securities in the first place.[85] That this division between banks and brokerages had already broken down by agency-led deregulation, to block a concurrent expansion of SEC authority to plug this new gap in the regulatory system effectively created a judicially-sanctioned loophole.

This pattern replayed itself several times in the late 1980s. As agencies deregulated New Deal era constraints on the financial sector, courts deferred citing agency expertise. For example, courts upheld the Fed's gradual erosion of Glass-

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[83] *Securities Industry Association v. OCC*, 577 F. Supp. 353 (DDC, 1983) (upholding Comptrollers' 1982 decision).

[84] *American Bankers' Association v. SEC*, 804 F.2d 739 (DC Cir. 1986), at 742-43. ("Rule 3b-9 proceeds on the premise that regulatory authority should be divided among government agencies according to the different financial functions performed by the regulated entity, and not according to the species of financial institution it is, as defined by its charter or even its primary function," but this is not the approach taken by Congress).

[85] *ABA v. SEC,* 804 F.2d, at 747.

Steagall's separation of investment and commercial banking in the 1980s, out of the "greatest deference" to their regulatory expertise.[86] But as these same agencies on occasion sought to expand their regulatory reach to cover new developments in the financial industry, courts often prevented these expansions of regulatory authority as transgressions of the formalist definitions of banking activities subject to agency oversight. Thus, Paul Volcker's Fed attempted in 1986 to expand its oversight of banks to cover new nonbank institutions that were based on new equivalents of demand deposits such as NOW accounts. These firms were not formally banks, and were not regulated as such, but the Fed instituted Regulation Y in 1984 to treat these entities as banks, since in practice they accepted financial instruments that operated like deposits.[87] This regulation was prescient in that much of the 2008 financial crisis involved a run on money-like demand deposits offered by nonbank entities, like money market mutual funds and repo contracts.[88] Yet the Supreme Court, consolidating several challenges to this regulation struck it down as it did the SEC's attempt to regulate bank-affiliated brokers. While the Fed explicitly attempted to regulate firms that were "functionally equivalent" to banks,[89] "no amount of agency expertise" could overcome the plain language of the Bank Holding Company Act of 1956, which defined banks to exclude the new

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[86] *Securities Industry Association v. Board of Governors of the Federal Reserve System*, 468 US 207 (1984); *Securities Industry Association v. Board of Governors of the Federal Reserve System*, 807 F.2d 1052 (1986).

[87] See Regulation Y, 49 FR 794 (1984); *Board of Governors of Federal Reserve System v. Dimension Financial Corporation*, 474 US 361 (1986) at 361-67.

[88] See Ricks, "Regulating Money Creation After the Crisis," 75.

[89] *Dimension Financial*, 474 US, at 373.

entities.[90] The Court even conceded the practical necessity of this kind of functionalist regulatory expansion, but felt bound by the terms of statute:

> Without doubt there is much to be said for regulating financial institutions that are the functional equivalent of banks. NOW accounts have much in common with traditional payment-on-demand checking accounts; indeed we recognize that they generally serve the same purpose. Rather than defining "bank" as an institution that offers the functional equivalent of banking services, however, Congress defined with specificity certain transactions that constitute banking subject to regulation. The statute may be imperfect, but the Board has no power to correct flaws that it perceives in the statute it is empowered to administer. Its rulemaking power is limited to adopting regulations to carry into effect the will of Congress as expressed in the statute.

Of course binding agencies to the scope of their delegated authority is an important principle in modern administrative law and a check on the power of the state. But what is interesting about these cases is the way in which the transposition of the problem of finance into a question of regulatory jurisdiction, expertise, and authority complicates the original challenge of financial regulation, often with problematic consequences. Thus, expert deference can sanctify deregulatory moves that proved problematic in retrospect. Meanwhile, the jurisdictional questions about the scope of agency authority oriented courts down a misleading path, resulting in the limiting of agency authority precisely where it was most needed in plugging growing cracks in the financial regulatory system resulting from innovations in new forms of nonbank money-like instruments, or the growth of securities affiliates outside the SEC's regulatory umbrella.

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[90] *Dimension Financial*, 474 US, at 368.

Federal versus local

A similar proxy debate over the scope of regulatory authority arises between federal and local regulators. Here too, the formal disputes are over the scope of authority on the part of national expert regulators like the OCC relative to state and local regulations on finance, but the animating concern is a substantive one. In recent years, for example, concerns about subprime lending played out in terms of this jurisdictional debate between national and local levels of regulation. The tendency in these clashes was to centralize authority away from local bodies into seemingly more expert-led and uniform regulatory agencies—which in effect undermined early efforts to respond to and head off the subprime crisis itself. Thus, as noted in Chapter 9 above, well before the subprime bubble collapsed, a number of cities like Oakland and Cleveland especially hard-hit by foreclosures and blight began to impose new regulations on the subprime lending industry. Yet each of these efforts were struck down as industry groups successfully litigated the local ordinances as being preempted by state and federal regulations.[91]

A similar dynamic appeared in context of federal-state preemption disputes. Prior to the 2008 financial crisis, the Court upheld in *Watters v. Wachovia* the OCC's preemption of state regulations on nationally-chartered bank mortgage business subsidiaries, striking down Michigan's attempted to impose regulations on a new mortgage subsidiary of Wachovia bank. In dissent, Justices Stevens, Roberts, and Scalia argued that the OCC ruling represented an overreach of agency authority over sovereign states.[92] Yet two years later, after the crash had

[91] See e.g., *City of New York v. American Financial Services Association*, 780 N.Y.S.2d 266 (NY 2004); *American Financial Services Association v. City of Cleveland*, 858 N.E.2d 776 (Ohio 2005).

[92] *Watters v. Wachovia Bank*, 550 US 1 (2007).

already occurred, the Court held that a similar OCC regulation purporting to preempt New York state's efforts to regulate banks was not a reasonable interpretation of the National Bank Act.[93] The difference between the two cases says less about the differences between Michigan and New York, and more perhaps about the heightened skepticism of the Court after the 2008 collapse of the OCC's pattern of favoring industry by overriding stricter state regulations on predatory lending.

Moral judgment and democratic institutions

In both the recent history of financial regulation and the post-crisis debates since 2008, there is a common tendency to turn to technocratic institutions as a preferred way to address controversial questions about what kinds of financial firms and activities we as a society ought to permit. But these are not purely technical issues to be resolved by neutral expertise. They fundamentally implicate moral judgments about what kind of economy we desire, and what kind of activities we value as a society. Furthermore, by transmuting these moral questions into technocratic ones to be judged by expert regulators, we do not resolve them. Instead, substantive concerns reappear through proxy debates over the scope of regulatory authority and expertise, creating an additional layer of formalism and contributing to some of the regulatory pathologies that helped fuel the 2008 crisis itself.

In the effort to avoid these moral controversies, policymakers and judges have routinely turned to centralized, national, expert-led organizations. By

[93] *Cuomo v. Clearing House Association*, 557 US 519 (2009).

contrast, a more moralized engagement with the substantive issues of economic regulation calls for a different institutional structure. Once engaged, such moral debate must be channeled through institutions where all affected interests can engage to voice their concerns, where there is a legitimate procedure through which these moral debates can be argued, judged, and revisited. A moralized understanding of economic regulation goes hand-in-hand with a more democratic structure for deciding these moral questions. This democratic structure reverses the features of technocratic governance described above. Instead of centralized, expert-led bodies, this democratic approach points us towards the kinds of democratized and decentralized governance institutions explored in Chapters 8 and 9 above.

11 DEMOCRATIC THEORY AND PRACTICE

Four years after the 2008 financial crisis, surprisingly little had changed in the financial industry. Wall Street profits had returned to pre-crisis levels while the sector as a whole remained concentrated in a few systemically-risky, too-big-to-fail firms. What has changed is the overarching system of financial regulation. After the reforms of the Dodd-Frank statute, all this financial activity now takes place under the watchful gaze of newly-empowered and expanded expert oversight through technocratic institutions like the Federal Reserve Board, the new Financial Stability Oversight Council, the SEC, and the new Consumer Financial Protection Bureau.

In appealing to the promise of technocratic regulation to mitigate market failures and promote economic welfare free of the corrupting influences of special interest or ordinary democratic politics, Dodd-Frank built on a well-worn tradition of progressive political thought, carrying forward the vision of Progressive and New Deal thinkers like James Landis. But in so doing, this turn to technocratic expertise also renewed the anxieties of laissez-faire critics who, at both ends of the twentieth century, warned against the dangers that state economic regulation would be co-opted and captured by special interest groups, and would therefore pose a threat to liberty. This criticism has also been a major thread of twentieth and now twenty-first century American politics, and has helped fuel a pervasive anxiety about the technocratic ideal.

We might have responded to the financial crisis differently. In contrast to this shaky ideal of expert management, there were a number of more radical, democratic possibilities that emerged in the face of the crisis itself. From reformers like Simon Johnson to protestors of the Occupy movement, a wide array of voices saw the problem of systemic risk and too-big-to-fail not as a technical matter, but as a moral problem of excessive private power—which in turn called for a more openly democratic response in which the voice of affected citizens and groups played a larger role than the occasional opportunity to provide input to expert regulators. These voices could have been fostered, bolstered, and engaged through a more democratic process of economic regulation, whether through greater leeway for city-level reform efforts, or through more structured modes of interest representation and participation in regulatory policymaking, implementation, and revision.

This kind of democratic approach to financial regulation may or may not prevent future financial crisis. It certainly would come with real costs as democratic decision-making is—and should be—tumultuous, conflictual, and iterative. But the appeal to self-correcting markets or apolitical experts is not costless either. Despite their veneer of frictionless optimization, both markets and experts are nevertheless inextricably implicated in networks and exercises of power and political influence. Nor do they possess the superior claim to mastery over economic conditions with which they are often attributed. The experts at the Fed and the forces of supply and demand are no more likely to devise the optimal crisis-preventing and welfare-enhancing economic orderings.

The most dangerous cost of this turn to markets or experts is a civic and political one. In delegating the governance of the economy to market systems or

insulated experts, we suffer a tremendous blow to our capacities as self-governing citizens. By transferring economic governance to the market or to experts, we place the locus of economic decision-making at a far remove from ordinary citizens out of a hope that this delegation will produce more effective and less corruptible governance at the price of our own disempowerment. It is a gamble we have been willing to make all too often, in financial reform and throughout the domain of modern economic policymaking. But it is a trade that we should think twice before making again. For all the justified concern over how our democratic politics functions today, rather than further narrowing the scope for citizens to govern themselves, we should instead seek to revive and rebuild democratic institutions to make them better able to grapple with the kinds of challenges posed by the financial crisis and economic upheaval more generally.

Indeed, the key cleavage throughout the previous chapters has been not between pro- and anti-regulatory views, but rather between two different visions of economic governance: the technocratic and the democratic. Both of these traditions have their origins in a critique of laissez-faire, but they take sharply different responses to these concerns about the market economy. Technocratic economic governance views the problem of the economy in technical, managerial terms, and thus turns to institutions that protect, encourage, and empower expert-led policymaking. The democratic approach, by contrast, sees economic governance as a fundamentally moral and political problem, a challenge not just of mitigating market failures and promoting economic welfare but of contesting exercises of private and market power, and of enhancing the agency of citizens to make their own lives. This in turn points to a different set of enabling institutions: not expert-led, but rather institutions that foster, catalyze, and make more

productive the agency of citizens themselves. This democratic approach shares with laissez-faire critics of the state an unease with technocratic authority, but rather than abandoning the regulatory project entirely, it seeks to reimagine economic governance as a fundamentally democratic task—a vehicle through which we as citizens collectively and continually work to address our shared economic and political challenges.

This turn to democracy, however, need not take the form of a blind optimism in democratic practice. We may be right to view with skepticism our current democratic institutions; the unease that technocratic and laissez-faire thought share over democratic politics does rest on an apt critique of democratic politics. But as with the critique of regulation, here too the answer lies not in abandoning the idea of democracy but rather in developing new institutions that provide more meaningful and effective channels for citizen agency. If we are serious about the moral challenges posed by the modern economy, and if we are committed to the value of individual and collective agency over our futures, then we must be willing to engage head-on controversial moral judgments about economic activities and economic structure as a democratic public, without wholly divesting ourselves of the capacities and responsibilities of making those judgments. We must in turn foster the spaces in which we can house and catalyze this kind of democratic judgment, whether through more participatory regulatory bodies or more empowered local ones. And while these democratic institutions and debates will assuredly require reformulation and revision, we must commit ourselves to the task of improving our democratic practice over time—rather than abandoning the democratic ideal in pursuit of the illusory stability, neutrality, and efficiency of market- or expert-based alternatives.

In the chapters above, I have suggested three possible avenues for democratic renewal: the repoliticization of our economic discourse, the transformation of regulatory agencies into sites of democratic practice, and the expansion of city governmental powers as meaningful spaces for democratic agency. These arguments do not offer precise institutional blueprints or policy prescriptions. Rather, they suggest some possible directions towards a revived democratic polity. What kind of institutional structures can empower and help mobilize citizens? How should be restructure our regulatory institutions to be more democratic? What are the prospects for meaningful local democracy? How can we approach decision-making in ways that engage the full range of moral, political, and technical concerns? These are the kinds of questions that democratic theory and democratic reform efforts must try to address.

From the growing innovation around Internet and social media based forms of participation, organizing, and crowdsourcing, to innovations in participatory governance such as the spread of participatory budgeting, to renewed efforts at preventing regulatory capture, there is no shortage of efforts at democratizing reform. Too often, these efforts alight on new tools of democracy—such as online participation—without an adequate political or social theory of what democracy entails and what we should be aiming for. At the same time, political theory by itself cannot outline a blueprint of democratic practice; the tensions, tradeoffs, and opportunities cannot be fully grasped in a vacuum. What we need is a greater interactive ferment between practically-rooted democratic theory on the one hand, and the actual practice and challenge of democratic reform on the other. Only through real-time experimentation, feedback, and reiteration that engages practitioners, reformers, social science, and normative theory can we develop our

ideas of how democratic agency can be realized. Political theory serves not as a blueprint or an articulation of an ideal, but rather as a way of engaging in diagnosis and critique, and as a way of making sense of, in real-time, the practices and institutions we innovate in practice.

This role of theory as embedded in, rather than distanced from, the world of democratic practice raises another latent theme of this project. In arguing for a more democratic view of economic governance in contrast with the technocratic reliance on experts, the above chapters also raise implications for our own claims to expertise as academics and political theorists. Just as economic policy questions cannot be fully addressed by experts from on high, who must instead be embedded in a thicker practice of democratic debate and experimentation, so too must contemporary social science and political theory embed itself in this broader democratic dialogue.

Many of the ideas discussed above have been inspired by the thought of Progressive Era radicals, notably John Dewey and Louis Brandeis. Neither figure offered a systematic normative theory of democracy, nor did they offer determinate policy prescriptions. By the standards of contemporary social science and political theory, neither thinkers' work would pass much muster. But both thinkers were deeply rooted in the politics and practice of Progressive Era reform politics, from the antitrust movement to urban social reform to education. The same can be said about other scholars of the period, from lawyers like Robert Hale and Morris Cohen to Progressive economists like Richard Ely and E. R. A. Seligman. It was from this rootedness that these scholars drew moral force, conviction, and insight.

The position of academic social science during the Progressive Era was unique and historically contingent. Professional social science came into being

during this period through a deep symbiosis with the aspirations of the reform movements. Even the formation of the first academic professional organizations like the American Economic Association or the American Political Science Association were premised on the public purpose of research in shaping social reform. This reformist ethic faded in large part due to political pressure that led many reformers to abandon more aggressive substantive reform proposals in favor of more conservative policies, advocated through the more neutral veneer of expert-driven social science.[1] These scholars stopped short of articulating a full moral vision of freedom, instead resorting to an appeal to empirical research and more rational public policy reasoning.[2]

Today's academia looks very different, having accepted this role of the dispassionate, neutral expert who stands apart from and above the rough and tumble of reform politics. But while the pursuit of knowledge is important, it is also important to recognize that this ethic of expertise is partly a product of a concerted effort to sterilize the research community of their political roots. This retreat to expertise highlights another contribution of Progressive Era thought. Not only did the thinkers of this period point to a kind of rich democratic renewal that we might benefit from today; they also exemplified, for a brief moment, an ethical ideal where the theory and practice of democracy were tightly bound together. If we are to overcome the challenges of the modern market economy,

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[1] Mary Furner, *Advocacy and Objectivity: A Crisis in the Professionalization of American Social Science, 1865-1905* (Transaction Publishers, 2010); Kenneth Finegold, *Experts and Politicians: Reform Challenges to Machine Politics in New York, Cleveland, and Chicago* (Princeton: Princeton University Press, 1995), 26-29; Daniel Rodgers, *Atlantic Crossings: Social Politics in a Progressive Age* (Cambridge: Harvard University Press, 1998), 100-5.

[2] Morton Horwitz, *The Transformation of American Law, 1870-1960* (New York: Oxford University Press, 1992), 208-12.

and develop institutions that provide meaningful democratic political agency, we would do well to follow that example.

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