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Deregulation, Reregulation, and the Myth of the Market

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DEREGULATION, REREGULATION, AND THE MYTH OF THE MARKET

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The last two decades have taught us a new word—deregulation—and the question of this symposium is whether the coming years are about to teach us yet another one—reregulation. To answer this question, however, it is necessary to determine what we mean by these two evocative but uncertain terms. The first, which is by now familiar, describes a social movement and a social theory, but it also characterizes the things that it describes. Like all characterizations, it rests upon a vision of the world, a vision that is rarely made explicit by the movement it indentifies. This vision involves strong claims about social organization, individual behavior, and political action. Whether there is a countervailing movement or a countervailing theory remains to be determined. But by using the term "reregulation" to describe that possibility, we clearly participate in the established vision of its predecessor. That is not necessarily fatal to the enterprise, of course; our culture is filled with important contributions by nonconformists, nonbelievers, anti-Federalists, antislavery advocates, deconstructionists, deregulators themselves, and many others who have defined themselves by what they have opposed. The important point is to discern the vision that lies behind terms like deregulation or reregulation, to trace its contours, and to bring its implicit assertions to light.

This Article pursues that inquiry, using the financial services industry as an example. Part I discusses recent events in the financial services industry, organizing these events in accordance with our common understanding of the terms deregulation and reregulation. It turns out that there are many events that fall within each category, and that the two groups cannot be ordered in any neat, temporal succession. One way to interpret this somewhat ragged pattern would be to look at the events in greater detail, while retaining the same set of categories. The approach that this Article adopts, however, is to examine the implications of the categories themselves. Part II does so, demonstrating that the terms deregulation and reregulation imply a particular vision of social organization, human behavior, and the polity. In addition, Part II examines the relationship between this vision and the discipline of economics, since economics has been the major source of our current theories about regulation. Part III then criticizes the vision that underlies deregulatory-reregulatory discourse as being based on assumptions that lack empirical support. This vision, Part III argues,

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may not be demonstrably wrong, but it is not demonstrably correct. Rather, it is one way of looking at, or interpreting, a certain group of events, and must be evaluated according to its usefulness as an interpretation. Part IV then suggests a process of evaluation that would encompass a variety of alternative visions, including the deregulatory one. It concludes by exploring the relationship of this process to economics. The observation is that alternative visions do not necessarily reject economics, and may actually expand its applications, although these alternatives deny economics the definitive effect on policy that is implicit in the deregulatory model.

I. Recent Events in the Financial Services Industry

A. Deregulation

Apart from the transportation industry, the financial services industry probably constitutes the clearest example of the process which we call deregulation. In financial services, this process has proceeded on three fronts: the elimination of interest rate restrictions, the reduction of geographic barriers to interstate banking, and the more gradual reduction of the separation between banking and other businesses. Since H. Helmut Loring and James M. Brundy have thoroughly described the process in a prior issue of this review,[1] the present discussion is restricted to broad outlines.

In 1933 Congress prohibited interest payments on demand deposits and authorized the Federal Reserve Board to limit interest payments on time deposits.[2] Sustained increases in interest rates during the 1970s led to a determined search for financial instruments and legal stratagems to circumvent these limitations. The NOW (negotiated order of withdrawal) account, essentially a demand deposit account operating under an alias,[3] and the money market account, a similarly disguised savings account offered by an investment or securities company,[4] were the products of these efforts. Congress could have shored up the existing restrictions by proscribing both devices, but it would have risked the fury of its inflation-sensitized constituency. Instead, it hesitantly began authorizing NOW accounts within defined geographic areas.[5] In 1980, as part of the Depositary Institutions Deregu-

1. Loring & Brundy, *The Deregulation of Banks,* 42 Wash. & Lee L. Rev. 347 (1985).

2. Banking Act of 1933, Pub. L. No. 73-66, 48 Stat. 162 (1933) (codified at 12 U.S.C. § 371 (1982) (superseded)).

3. On the evolution of NOW accounts, see Riordan, *Negotiable Orders of Withdrawal,* 30 Bus. Law. 151 (1974); Note, *Negotiable Order of Withdrawal (NOW) Account: "Checking Accounts" for Savings Banks?,* 14 B.C. Indus. & Com. L.R. 471 (1973).

4. On money market accounts generally, see K. Cooper & D. Fraser, Banking Deregulation and the New Competition in Financial Services 5-7 (1984); R. Litan, What Should Banks Do? 33-35 (1987).

5. Act of Aug. 16, 1973, Pub. L. No. 93-100, § 2, 87 Stat. 342 (1973) (authorizing NOW accounts in Massachusetts and New Hampshire); State Taxation of Depositories Act,

lation and Monetary Control Act ("DIDMCA"),[6] Congress abolished the restriction on demand deposits and provided for phased-in elimination of the restriction on time deposits. When this proved insufficient to halt the growth of nonbank money market funds, it followed with the Garn-St. Germain Act,[7] which permitted banks to offer money market accounts on essentially the same terms as their competitors. With that, the elimination of interest rate restrictions was essentially complete.

The reduction of the barriers to interstate banking has been initiated by a different and more unexpected actor—the state legislatures. Geographic barriers to interstate banking were maintained by two well-known federal laws, the McFadden Act, which applies to interstate branching by national banks,[8] and the Douglas Amendment, which applies to the interstate activities of bank holding companies.[9] Neither of these Acts prohibits interstate banking; they merely empower the states to prohibit it if they so choose. For a long time, virtually every state made use of this power, the small states to protect their banking industry from larger neighbors, the larger states to protect their banking industry from New York. As funding difficulties grew in the 1980s and credit began to run short, it finally dawned upon state legislators that they might be protecting their state banks at the expense of all their other industries. Maine and Alaska were the first to abandon their dreams of becoming worldwide financial centers, and to invite banks headquartered in other states to do business within their borders.[10] During the next few years, the great majority of states followed the same path.[11] Texas, still nourishing itself on the myth that it is an independent

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Pub. L. No. 94-222, § 9, 90 Stat. 197 (1976) (extending authorization to Connecticut, Maine, Rhode Island and Vermont); Financial Institutions Regulatory and Interest Rate Control Act of 1978, Pub. L. No. 95-630, § 1301, 92 Stat. 3712 (1978) (codified at 12 U.S.C. § 1832) (extending authorization to New York); Act of Dec. 28, 1979, Pub. L. No. 96-161, § 106, 93 Stat. 1235 (1979) (codified at 12 U.S.C. § 1832 (1982)) (extending authorization to New Jersey).

6. Pub. L. No. 96-221, 94 Stat. 132 (1980) (codified as amended at 12 U.S.C. §§3501-24 (1982)). For the provision in question, see *id.*, tit. III, § 302(a) (codified at 12 U.S.C. § 371a (1982)). *See generally* T. CARGILL & G. GARCIA, FINANCIAL DEREGULATION AND MONETARY CONTROL (1982); K. COOPER & D. FRASER, *supra* note 4, at 105-25.

7. Pub. L. No. 97-320, 96 Stat. 1469 (1982); *see id.* § 326, 96 Stat. at 1500-1501 (codified at 12 U.S.C. § 3503(c) (1982)). Current rules on deposit account interest appear at 12 C.F.R. §§ 217, 329. On Garn-St. Germain generally, see K. COOPER & D. FRASER, *supra* note 4, at 126-42; D. FRASER & J. KOLARI, THE FUTURE OF SMALL BANKS IN A DEREGULATED ENVIRONMENT 53-67 (1985).

8. McFadden Act, ch. 191, 12 U.S.C. §§ 36, 81 (1982).

9. Bank Holding Company Act of 1956, ch. 240, 12 U.S.C. §§ 1841-185 (1982). Section 1842(d)(l) is the Douglas Amendment, so named after its sponsor, Senator Paul Douglas of Illinois.

10. ALASKA STAT. § 06.05.235 (Supp. 1984); ME. REV. STAT. ANN. tit. 9-B, § 1013 (Supp. 1984). At approximately the same time, Delaware and South Dakota authorized certain banking activities by out-of-state banks, but these statutes were designed to attract new jobs without removing the protection for existing state banks. *See* DEL. CODE ANN. tit. 5, §§ 801-826 (1974); S.D. CODIFIED LAWS ANN. §§ 51-16-40, -41 (1984).

11. *See* Frieder, *The Interstate Banking Landscape: Legislative Policies and Rationale,* 6

country, suddenly found that the drop in oil prices was fast reducing it to the reality of lesser developed country and unexpectedly joined the general trend.[12] This state legislation, combined with Garn-St. Germain's reluctant authorization that out-of-state institutions can purchase failing thrifts, has virtually eliminated the legal barriers to interstate banking.

Elimination of the regulatory barriers that separate banking from other financial activities such as securities dealing, brokerage, investment services, insurance, and from commerce generally, has proceeded the most gradually of these three forms of deregulation, although, or perhaps because, the largest number of actors have participated in the process. Some state legislatures have authorized their state-chartered banks to engage in previously prohibited activities.[13] The federal regulators have done the same with the national banks and bank holding companies, enthusiastically in the case of the ever congenial Comptroller of the Currency, reluctantly in the case of the dragon-like Federal Reserve.[14]

The precincts that have been most frequently violated by the federally-authorized incursions are those of the securities industry. Almost every time these incursions occur, the Securities Industry Association or the Investment Company Institute has sued the relevant regulator with the result that the federal courts have been drawn into the deregulatory fray. As it turns out, these courts, and particularly the United States Supreme Court, have the clearest policy of any federal actor; making use of deference to federal agencies, hard looks at federal agencies, strict construction, loose construction, original interest, and evolutionary meaning, the federal courts have consistently ruled in favor of deregulation, usually by a unanimous vote.[15]

CONTEMP. POL. ISSUES 41 (1988). According to Frieder's survey, 42 states (including the District of Columbia) have enacted some form of interstate banking law. Of these, 16 are fully national, while the remaining 26 are regional (but, in 11 cases, have provisions for conversion to a national authorization). The Supreme Court upheld the constitutionality of regional banking laws in Northeast Bancorp, Inc. v. Board of Governors, 472 U.S. 159 (1985). *See* Miller, *Interstate Banking and the Court,* 1985 SUP. CT. REV. 179.

12. TEX. STAT. ANN. art. 343-916 (Vernon Supp. 1988).

13. *See, e.g.,* CAL. FIN. CODE §§ 751-753, 772, 1338 (West Supp. 1985) (allowing banks to underwrite mutual funds, participate in real estate development, and underwrite securities); *id.* at § 6702 (allowing unlimited investment by savings and loan institutions in nonmortgage assets); S.D. CODIFIED LAWS ANN. § 51-18-1.3 (Supp. 1988) (allowing banks to sell and underwrite insurance outside South Dakota); TEX. STAT. ANN. art. 342-114 (Vernon Supp. 1985) (allowing unlimited investment by savings and loan institutions in nonmortgage assets).

14. *See, e.g.,* ICI v. Conover, 596 F. Supp. 1496, 1499-50 (D.D.C. 1984) (describing comptroller's ruling on individual retirement accounts), *aff'd,* 790 F.2d 925 (D.C. Cir.), *cert. denied,* 107 S. Ct. 421 (1986). Decision of the Comptroller of the Currency in *In re* American National Bank of Austin (Sept. 2, 1983) (authorizing national banks to engage in full service brokerage); Bankers Trust New York Corporation, 73 Fed. Res. Bull. 138 (1987) (authorizing bank holding company to deal in commercial paper, subject to restrictions); Citicorp, 70 Fed. Res. Bull. 149 (1984) (authorizing bank holding company to acquire savings and loan, subject to restrictions).

15. *See, e.g.,* Clarke v. SIA, 107 S. Ct. 750 (1987) (unanimous result) (permitting bank holding company to open discount brokerage offices interstate); SIA v. Board of Governors,

Congress has been much less clear in its direction. A full account of its august peregrinations on bank product expansion would fill this entire volume. For at least ten years preceding 1987, everyone but Congress agreed that Congress should act, but no one agreed what Congress should do, and so Congress did nothing. Finally, it responded to a sense that the entire financial system was unravelling beyond all possible repair, and slapped a one-year, across-the-board moratorium on all federal deregulatory action. This Act of Desperation was known, somewhat risibly, as the Competitive Equality Banking Act of 1987.[16] In the year that followed, however, the hoped-for enlightenment did not descend upon Congress; although major bills were introduced, the moratorium nonetheless expired without new legislation. The federal regulators were now required to address themselves to the mountain of applications that had accumulated on desks during the period of the moratorium. The federal regulators were back where they started. Even before the moratorium ended, the Securities Industry Association had filed suit once more, based on what the regulators said they planned to do.[17] With the situation unravelling once more, Congress seemed to lapse into a state of political shock, and, to date, has failed to act on any of the legislative proposals that have been presented to it.

B. Reregulation

These events seem to reveal a clear, although somewhat spasmodic trend toward the repeal of regulatory rules—that is, a pattern of deregulation in the financial services industry. In fact, if one defines regulation in terms of the market structure provisions enacted between 1933 and 1970 involving interest rates, geographic boundaries, and product lines, the pattern is difficult to deny. But in the late 1960s, the financial services industry became subject to a new type of regulation. Congress, and to some extent the states, began enacting laws to protect ordinary consumers from the rigors of the

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468 U.S. 207 (1984) (unanimous decision) (authorizing bank holding company to operate discount brokerage service); Board of Governors v. ICI, 450 U.S. 46 (1981) (unanimous decision) (authorizing bank holding company to provide investment advisory services); SIA v. Board of Governors, 807 F.2d 1052 (D.C. Cir. 1986) (unanimous decision) (upholding Federal Reserve Board authorization of bank holding company's sale of commercial paper), *cert. denied,* 107 S. Ct. 3228 (1987); ICI v. Conover, 790 F.2d 925 (D.C. Cir.) (authorizing national bank to market trust for assets of individual retirement accounts), *cert. denied,* 107 S. Ct. 421 (1986) (unanimous decision); *cf.* Board of Governors v. Dimension Fin. Corp., 474 U.S. 361 (1986) (unanimous decision) (overturning Federal Reserve order closing nonbank bank loophold); Lewis v. BT Inv. Managers, Inc., 447 U.S. 27 (1980) (unanimous decision) (declaring unconstitutional Florida statute forbidding out-of-state bank ownership of investment advisory service). For the Supreme Court's attitude toward Glass-Steagall, see Langevoort, *Statutory Obsolescence and the Judicial Process: The Revisionist Role of the Courts in Federal Banking Regulation,* 85 MICH. L. REV. 672 (1987).

16. Pub. L. No. 100-86, 101 Stat. 489 (1987) (codified as amended at 31 U.S.C. § 3328 (1988)).

17. Securities Indus. Ass'n v. Board of Governors, 847 F.2d 890 (D.C. Cir. 1988); Securities Indus. Ass'n v. Board of Governors, 839 F.2d 37 (2d Cir. 1988).

credit and investment markets. The first of these enactments was the Truth-in-Lending Act of 1968,[18] which preceded the start of the deregulatory era by several years. But the bulk of this legislation came during the same period as the deregulatory actions just described, and seems to be an equally important trend moving in the opposite direction.

It is true that the Truth-in-Lending Act was modified in 1980, as part of the DIDMCA,[19] and that these modifications, called Truth-in-Lending Simplification, were regarded as part of the deregulation movement. But this legislation is properly described as corrective, not deregulatory. The original Truth-in-Lending Act was something of a botch; with the addition of the Federal Reserve Board's implementing regulations,[20] it proved so complex that creditors were simply unable to comply with it. As a result, many consumers who had complaints about the product that they acquired with their loan, or who were simply unable to meet their loan payments, could avoid their obligations by charging the creditor with Truth-in-Lending violations.[21] This interesting, if rather rough form of consumer redress was clearly beyond the intent of the Truth-in-Lending Act's proponents, and correcting it hardly represented a retreat from the basic protectionist idea. Even at the flood tide of the deregulation movement, Congress did not abandon Truth-in-Lending's central requirement that creditors disclose their terms. In fact, while in making the Truth-in-Lending Act possible to comply with, Congress actually strengthened some of its provisions.[22]

Apart from the vicissitudes of Truth-in-Lending, a steady stream of consumer protection regulation has been enacted during the last two decades. The 1970 amendments to Truth-in-Lending regulated the payment aspect of credit cards, allocating the bulk of fraud losses to the issuing bank.[23] The Fair Credit Billing Act of 1974 required creditors to provide regular account statements and to correct or explain those charges that the customer challenged.[24] The Fair Credit Reporting Act of 1970 imposed a number of substantive restrictions on credit rating agencies,[25] and the Fair Debt Col-

18. Pub. L. No. 90-321, tit. I, 82 Stat. 146 (1968) (codified as amended in 15 U.S.C. §§ 1601-1613, 1631-1641 (1982)).

19. Truth-in-Lending Simplification and Reform Act, Pub. L. No. 96-221, tit. VI, 94 Stat. 168-85 (1980) (codified at 15 U.S.C. §§ 1601-1646 (1982)).

20. Regulation Z, 12 C.F.R. § 226 (1988).

21. *See* Pettit, *Representing Consumer Defendants in Debt Collection Actions: The Disclosure Defense Game,* 59 TEX. L. REV. 255, 256-66 (1981); *see also* Landers & Rohner, *A Functional Analysis of Truth in Lending,* 26 UCLA L. REV. 711 (1979); Whitford, *The Function of Disclosure Regulation in Consumer Transactions,* 1973 WIS. L. REV. 400.

22. For example, a new provision, 15 U.S.C. § 1646, authorized the Federal Reserve Board to "collect, publish, and disseminate to the public . . . the annual percentage rates charged for representative types of non-sale credit." *See generally* Pettit, *supra* note 21; Rohner, *Truth in Lending "Simplified": Simplified?,* 56 N.Y.U. L. REV. 999 (1981).

23. Amendments to Truth in Lending Act, Pub. L. No. 91-508, tit. V, § 502(a), 84 Stat. 1126 (1970) (codified as amended at 15 U.S.C. §§ 1642-1645 (1982)).

24. Fair Credit Billing Act, Pub. L. No. 93-495, tit. III, § 306, 88 Stat. 1511 (1974) (codified at 15 U.S.C. §§ 1666-1666j (1982)).

25. Fair Credit Reporting Act of 1970, Pub. L. No. 91-508, tit. VI, § 607, 84 Stat. 1128 (1970) (codified at 15 U.S.C. §§ 1681-1681t (1982)).

lection Practices Act of 1977 did the same for collection agents.[26]

In the Equal Credit Opportunity Act of 1974, Congress prohibited the denial of credit on the basis of sex, race, or national origin.[27] It thus took the first step toward securing consumers' access to credit, rather than simply protecting consumers from abuse. This was followed in 1977 by the Community Reinvestment Act, which declared that banks had some sort of obligation to provide credit to the communities from which they obtained their deposits.[28] The precise nature of this obligation was left unclear, and the absence of realistic sanctions left that unclear obligation unenforceable. Nonetheless, there lay within this sloppy, toothless statute the possibility that the supply of credit would be regulated to assist the survival of small towns or the revival of blighted, urban neighborhoods.

All these statutes predate 1980, when Ronald Reagan, who explicitly had committed himself to deregulation, was elected by a landslide. Within a few years of his election, however, a new consumer protection initiative developed, this time to regulate the check collection system. The basis of this initiative was dissatisfaction with the bankers' practice of placing holds on deposited checks, or even cash, so that customers could not draw up their funds for several days or weeks. This was a long-standing practice, and there was no evidence of a precipitating crisis. But the consumer movement placed it at the top of its agenda; within a few years several states had enacted funds availability laws,[29] and there was a clear majority in both houses of Congress for federal legislation.[30] The actual legislation did not pass until 1987, largely because it was attached to more controversial measures.[31] But when it did, it contained a surprise. Congress had not only imposed severe restrictions on banks' funds availability practices, with elaborate disclosure requirements, but it had authorized and encouraged the Federal Reserve Board to regulate the entire check collection system. Furthermore, it had done so without anyone's urging, and over the explicit objections of the agency charged with implementing these regulations.[32]

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26. Fair Debt Collection Practices Act of 1977, Pub. L. No. 95-109, tit. VIII, §§ 803-817, 91 Stat. 874 (1977) (codified at 15 U.S.C. §§ 1692-1692o (1982)).

27. Equal Credit Opportunity Act of 1974, Pub. L. No. 94-239, §§ 3(a)-7, 90 Stat. 251 (1976) (codified at 15 U.S.C. §§ 1691b-1691f (1982)).

28. Community Reinvestment Act of 1977, Pub. L. No. 95-128, tit. VIII, §§ 802-806, 91 Stat. 1147 (1977) (codified at 12 U.S.C. §§ 2901-2905 (1982)).

29. *See e.g.,* CAL. COM. CODE §§ 4212, 4213 (West Supp. 1983); CAL. FIN. CODE §§ 865-867 (West Supp. 1988); FLA. STAT. ANN. § 655.081 (West 1984); N.Y. BANKING LAW § 14-d (McKinney Supp. 1988). *See generally* Cooper, *Checks Held Hostage—Current Legislation on Funds Availability,* 103 BANKING L.J. 4, 4-15 (1986).

30. *See* 1986 Cong. Q. 2683 (support for funds availability legislation, and complexities of enactment); Cooper, *supra* note 29, at 15-28 (summarizing content of congressional bills).

31. Expedited Funds Availability Act of 1987, Pub. L. No. 100-86, tit. VI, § 602-611, 101 Stat. 635 (1987) (codified at 12 U.S.C. §§ 4001-4010 (Supp. 1988)).

32. *Id.* § 4009(b), (c). For a discussion of the Act's Effects on the payment system, see Cooter & Rubin, *Orders and Incentives as Regulatory Methods: The Expedited Funds Availability Act of 1987,* 35 UCLA L. REV. 301, 334-36 (1988).

This past term the growth of consumer protection regulation has continued apace. The Fair Credit and Charge Card Disclosure Act of 1988 was enacted, adding to existing Truth-in-Lending requirements for credit card debt.[33] The Senate passed a Home Equity Loan Act, requiring extensive disclosures on loans secured by previously purchased real estate.[34] In addition, both houses passed a Truth-in-Savings Act, requiring the disclosure of yield rates on investment accounts. The only reason final legislation did not pass was that the Truth-in-Savings Act was included in the Senate's controversial deregulation bill,[35] a bill also contains an effort to implant some teeth into the Community Reinvestment Act.[36] Consumer advocates regard this latter effort as a quid pro quo for their support of bank product expansion, and that support may well be necessary for the general bill to pass.

Thus the pattern that emerges from the recent regulatory history of the financial services industry is too complicated to be captured by a single term. There certainly have been a number of events that can be properly regarded as "deregulatory," but there are numerous others that appear to move in the opposite direction. In general, the deregulatory efforts involve elimination of the restrictions upon market structure, those restrictions designed to distinguish demand deposits from savings accounts, to separate one state's banks from another's, and to separate banks in general from other kinds of institutions.[37] By contrast, new regulations have been imposed to protect consumers from oppressive practices, to inform them of contractual terms, and to ensure them a supply of credit. The question is whether these events can be fit within a single framework of analysis—whether the second set of events are usefully regarded as reversing the same process that the first set has initiated.

II. The Deregulatory Vision

Our efforts to make sense of recent events in the financial services industry are strongly affected by the vision that is embedded in the terms

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33. P.L. No. 100-464, 102 Stat. 2271 (1988).

34. S. 1886, 100th Cong. 2d Sess., tit. VII (1988); *see* 134 Cong. Rec. S. 3437 (daily ed. March 30, 1988) (record of passage); *id.* at S. 3520, 3538-40 (daily ed. March 31, 1988) (text of provision enacted as Title VII of Proxmire Financial Modernization Act of 1988). The vote was 94 in favor, 2 opposed, 4 not voting. *Id.* at 3437.

35. S. 1886, 100th Cong. 2d Sess. tit. VI (1988); *see* 234 Cong. Rec. S. 3437 (daily ed. March 31, 1988) (record of passage); *id.* at S. 3520, 3536-38 (daily ed. March 31, 1988) (text of provision enacted as Title VI of Proxmire Financial Modernization Act of 1988).

36. S. 1886, 100th Cong. 2d Sess., § 914, 34 Cong. Rec. S. 3543 (daily ed. March 31, 1988) (requiring Federal Reserve Board approval under Community Reinvestment Act, for bank holding company applications to engage in nonbanking, as well as banking activities).

37. There are, however, further complexities in the pattern. For example, recent efforts to tighten capital requirements can be seen as increased regulation of structural requirements. *See* International Lending Supervision Act of 1983, 12 U.S.C. §§ 3901-3912 (1982 & Supp. IV 1986); 12 C.F.R. § 325.3 -.4 (1988) (FDIC); 12 C.F.R. §§ 208, 225, 263 (1988) (Federal Reserve Board); 12 C.F.R. §§ 3.5-.21 (1988) (Office of the Comptroller of the Currency).

deregulation and reregulation. This vision is not really contained in the words themselves, of course, but it is implicit in the way these words are used within our social context. It strongly affects, and perhaps controls, its proponents' image of society, of individual behavior, and of the political system. Economic analysis is regularly linked with this vision, lending it a distinctive, and apparently empirical character. As a result, discussions of deregulation tend to focus on the role of economic analysis, and on its validity as social science. The effort here, however, is to explore the vision itself; while this vision often determines the way economics is used in law and public policy, it is not derived from economic analysis and it is certainly not equivalent to such analysis.

A. Society

One element of the vision that the terms deregulation and reregulation imply is that there exists a natural form of social organization where regulation has not been imposed. This is, of course, the "free market," where willing buyers and willing sellers exchange goods, services, and money according to mutual agreements.[38] The free market is often treated as a natural implication of two other premises: that individuals are motivated by self-interest, and that the polity society is not a collective entity, with a general will, but a collection or alliance of these individuals. In other words, given these kinds of individuals, and this kind of society, it is argued that a market naturally follows as the best form of social organization. But the free market is, in fact, a preempirical and pretheoretical image that underlies these premises about individuals and the polity. It is the master premise, an independent, unarticulated concept of a good society that silently controls the views of its proponents about both individuals and political organizations.

To begin with, the free market image controls its proponents' views about the proper role of the state, and the proper scope of regulation. The role of the state, according to the free market view, is to enforce agreements between individuals according to their terms and—just as importantly, but generally less often mentioned—to create and control the money that is used for payment. Any other governmental involvement is an offense against the purity of the market. "Deregulation," as we use the term, refers to the removal of such involvement, a restoration of the market to its natural state. "Reregulation" refers to the reintroduction of those rude intrusions, and thus carries with it a vague air of backsliding or loss of nerve.

This does not mean that regulation always is regarded as a mistake. But implicit in this market vision is the idea that regulation is an unnatural

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38. Proponents of deregulation who make this assumption, with varying degrees of explicitness, include S. Breyer, Regulation and Its Reform (1982); B. Mitnick, The Political Economy of Regulation: Creating, Designing and Removing Regulatory Forms (1980); A. Stone, Regulation and Its Alternatives 10-13, 35-60 (1982); F. Thompson & L. Jones, Regulatory Policy and Practices: Regulating Better and Regulating Less 8-43 (1982); L. White, Reforming Regulation: Processes and Problems (1981).

act that should only be undertaken for a specified and carefully articulated reason. The free market, in other words, is a presumption, a preferred approach, while regulation must bear the burden of justification. What justifies regulation, according to this view, is market failure, that is, the failure of the market to achieve efficiency.[39] The purpose of that regulation must be restoration of the market to its natural condition, or to as close an approximation of that condition as can be hoped for in these fallen circumstances. Typically, this involves elimination of monopoly, adjustment for externalities, or correction of serious information asymmetries.[40] The characterization of these phenomena as market failures, and the prescriptions for their resolution, are based upon the vision of the market as a natural state of social organization.

Economics is linked to this free market vision for at least two reasons. In its classic form, economic analysis demonstrates that a free market will maximize wealth,[41] while a regulated market, one in which the government intervenes for reasons other than the correction of market failure, will not.[42] Traditionally, many regulations were justified in terms of their ability to produce wealth, but the analysis indicates that they will not do so as effectively as the abandonment of regulation. Economic analysis thus served as an engine of the Enlightenment, which demanded that all social rules that could not be justified in terms of real world effects be cleared away.[43]

More recently, mathematical economics has demonstrated that a free market can be modeled, and has produced the first social science theory that possesses the ardently desired qualities of prediction and precision that we associate with natural science.[44] Regulation prevents the model's operation. An effort has been made to bring regulatory action within the model, by means of public choice theory, but the result, however interesting, is not quite satisfactory. While public choice may explain certain political behaviors by treating them as market phenomena, it cannot prevent those behaviors from altering the market for goods, services, and money in a manner that disables the mathematical theory. Thus, traditional economics demonstrates that a free market serves the widely accepted social purpose

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39. *See* K. MEIER, REGULATION: POLITICS, BUREAUCRACY AND ECONOMICS (1985); B. MITNICK, *supra* note 37, at 2; R. LITAN & W. NORDHAUS, REFORMING FEDERAL REGULATION 36 (1983) (stating "traditional view").

40. *See* S. BREYER, *supra* note 37, at 15-28; A. STONE, *supra* note 37, at 61-166; F. THOMPSON & L. JONES, *supra* note 37, at 44-92.

41. Myrdal, *Implicit Values in Economics,* in THE PHILOSOPHY OF ECONOMICS 252 (Hausman ed. 1984). The wealth maximizing nature of perfectly competitive markets is often described in terms of "social optimality" or "pareto efficiency." *Id.; see* R. COOTER & T. ULEN, LAW AND ECONOMICS 44-45 (1988).

42. *See supra* note 37 (citing proponents of deregulation).

43. R. ANCHOR, THE ENLIGHTENMENT TRADITION 7 (1967); I. SCHNEIDER, THE ENLIGHTENMENT 19-21 (1965).

44. For a critique of economists' claims to predictive accuracy, see D. MCCLOSKEY, THE RHETORIC OF ECONOMICS 15-16 (1985).

of wealth maximization, and modern economic models are then constructed upon the existence of that market.

B. Individuals

A second element of the deregulatory vision, and an implication of its major element of a naturally-occurring market, is that individuals must behave in a particular manner. This behavior can be termed autonomous self-interest—that individuals are primarily motivated by the desire to maximize their material condition. In order to produce a market, the desires involved must preexist culture,[45] and must be material in character.[46] If culture can determine the self-interest that people perceive, the only assertion being made is that people interact with their culture by internalizing cultural norms. Self-interest would then be a method of social control, not an independent human behavior that is controlled by means of regulation. As such, it would be malleable by social systems; individuals could believe that anything, including behaviors diametrically opposed to wealth maximization, constituted their personal self-interest. Similarly, the market image requires that self-interest focus on the kinds of rewards that a market, that is, the exchange of goods and services, can provide. If self-interest can be non-material, for example, if altruistic behavior is self-interested because it satisfies one's personal interest in benefiting others, the entire concept collapses into the empty observation that people want to act in accordance with their own desires.[47] The underlying image of deregulation is much more definitive; it suggests that there exists an independent set of desires that market exchanges satisfy—the desire to maximize an autonomously created and materially defined self-interest.

This theory of behavior is regarded as a real universal, true in all cultures and in all ordinary circumstances. Left undisturbed, the argument goes, it will dominate material interactions between individuals; suppressed, it will assert itself in black markets, corruption, insincere exceptions, and official circumventions. Regulation, as a form of such suppression, is unnatural according to this vision because it interferes with basic human nature, as well as with the market. Regulation can be justified where the market fails, but in other cases it should be avoided.

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45. *See* Boulding, *The Basis of Value Judgments in Economics*, in HUMAN VALUES AND ECONOMIC POLICY 71-2 (Hook ed. 1967); Nagel, *Preference, Evaluation, and Reflective Choice*, in HUMAN VALUES AND ECONOMIC POLICY 77 (Hook ed. 1967) (taking preferences as precultural is unrealistic, but useful assumption).

46. *See, e.g.*, S. KELMAN, WHAT PRICE INCENTIVES: ECONOMISTS AND THE ENVIRONMENT 20-21 (1981). "Material" in this context does not mean "tangible." "Material interests" include interests in, at least, goods and services. In fact, defining what counts as a material good is somewhat difficult. The general idea is that a material desire relates to the material, as opposed to the spiritual conditions, of one's own life. *Id.*

47. *See* Sen, *Rational Fools: A Critique of the Behavioral Foundations of Economic Theory*, 7 PHIL. & PUB. AFF. 317 (1978).

The precise relationship between an asserted human universal like self-interest and a normative argument, like the presumption against regulation, is complex. To simplify, there are at least two significant connections. First, a social policy that runs counter to natural human instincts is likely to be ineffective, or to require so much force to effectuate that the policy would be unacceptable on independent grounds. Second, real universals carry with them an implicit normative appeal, stemming from our general respect for human nature. Many normative systems are based upon such claims. There is no logical argument that such universals imply normative arguments, but the normative arguments seem quite persuasive if one accepts the universal.

Again, economic analysis has close connections with the concept of human nature that underlies our deregulatory discourse. Economics tells us how individual welfare can be maximized, and thus is closely linked to a motivation structure based on rational self-interest. Of course, no serious economist would deny that even the most rational, egoistic individuals have other desires besides their own welfare. Economic theory, however, applies most directly and usefully to material welfare; the more central material welfare is to peoples' motivation structure, therefore, the more important economic analysis becomes. Moreover, mathematical economics depends upon rational, self-interested behavior. At present, economics cannot model the actions of the altruistic or the self-destructive, and it encounters serious difficulties with even garden-variety irrationality.[48]

B. Politics

The deregulatory vision of a naturally-occurring market, and of self-interested individuals leads, in turn, to a theory of politics. Since human beings are autonomous individuals, with preexisting preferences, conflicting desires, and self-interested motivations; society is thus an uneasy alliance among natural antagonists. For over three hundred years, we have conceptualized this alliance as a type of contract, whereby these autonomous individuals exchanged part of their independence for advantages that could be secured only by collective action.[49] Thus, individuals are viewed as anterior to society, and the political system they have created is to be judged by the extent to which it satisfies or frustrates their preexisting desires.

A common assumption is that the virtues of the market, and thus the vices of regulation, can be derived from this theory of individuals and of

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48. H. KATOUZIAN, IDEOLOGY AND METHOD IN ECONOMICS (1980); *see also* J. ELSTER, ULYSSES AND THE SIRENS: STUDIES IN RATIONALITY AND IRRATIONALITY 141-6 (1979).

49. The basic texts, which are almost too familiar to require citation are T. HOBBES, LEVIATHAN (F. McNeilly rev. ed. 1968); J. LOCKE, THE SECOND TREATISE OF GOVERNMENT (J. Gough rev. ed. 1946). Significantly, Part I of Hobbes' book is entitled "Of Man," and Part II is "Of Commonwealth." Similarly Locke begins with the state of nature (ch. II), and reaches "Civil Society" only in Chapters VII and VIII. For modern political theories built on contract doctrine, see J. BUCHANAN & G. TULLOCK, THE CALCULUS OF CONSENT (1962); J. RAWLS, A THEORY OF JUSTICE (1971).

politics. In fact, the reverse is true; the vision of politics rests on the belief in the market as a natural form of social organization, as well as on a belief in autonomous, self-interested individuals. Society gets started, after all, when individuals who exist without society join together in a contractual agreement. But how did these individuals know what a contract was, and how to go about negotiating one, particularly a complex one like The Social Contract?[50] The only answer is that contractual behavior comes naturally to human beings, or that these human beings, even in their feral state, were living in a natural market of some sort. Of course, proponents of the contract theory regard it as a conceptual construct for analyzing political morality, not as an actual account of social history. But social contract theory presents the same basic difficulty on the conceptual level as it does on the historical one. Contracts must be formed according to a set of rules, and are deemed enforceable and binding on the parties only because of the rules' continuing vitality. Even acknowledging the social contract to be a theoretical construct, where do the rules that govern the social contract come from? Presumably, they are part of some conceptual ground state, some natural morality that is regarded as preexisting the society that has been created in accordance with the rules.

There is a second reason why this vision of the political system as a means of satisfying individual desires depends upon the vision of a naturally-occurring market. In essence, the idea that the purpose of politics, or of society in general, is to satisfy the conscious choices of individuals is a market image. Even the liberal tradition does not limit society's role to this market image; rather, it embraces other views that recognize an educative or emancipatory role for social life. The belief in the superiority of the market also involves strong assumptions about which preferences should be satisfied. Members of a society may have individual preferences that can be satisfied through a market, but they also have social preferences that can be satisfied through collective, governmental action, including market regulation. The only apparent reason to favor one set of these preferences over another is that the market preferences are regarded as natural ones, and thus more real than other preferences. Of course, the market is capable of registering the intensity, as well as the existence of people's preferences, but so is a pluralist democracy.

The same set of attitudes underlie the deregulatory approach to ordinary politics, as well as to political theory. The market image, once more, is that human beings are naturally motivated by autonomous self-interest.[51]

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50. *See* T. GREEN, LECTURES ON THE PRINCIPLES OF POLITICAL OBLIGATION 66 (P. Harris & J. Morrow ed. 1986); C. MACPHERSON, THE POLITICAL THEORY OF POSSESSIVE INDIVIDUALISM: HOBBES TO LOCKE (1962). This same criticism has been advanced in slightly different form with regard to Rawls' theory. *See* Nagel, *Rawls on Justice,* in READING RAWLS 5 (N. Daniel ed. 1975). For the idea that the nature of the social contract will depend on the way in which the choice situation is defined, see B. ACKERMAN, SOCIAL JUSTICE AND THE LIBERAL STATE 337-42 (1980).

When this image is extended to public officials, as well as to market participants, it suggests that legislators generally try to maximize their chance of reelection, while bureaucrats try to maximize their power, or minimize the threat to their existing power. Citizens will organize to obtain favorable treatment from these self-interested officials, but only to the extent that the advantages to be obtained exceed the cost of organizing. As a result, special interest groups, where the individual members' stakes are high and their numbers are relatively low, will organize effectively, while the general public, whose stakes in any given issue are low and whose numbers are high, will not.[52] Legislators, in their effort to be reelected, consequently will respond to special interests rather than the interests of the general public. This view of politics, which generally is called public choice, is directly derived from the view that the market is the natural form of social organization. In effect, it postulates that political life is really a market for reelection, or agency funding, rather than a collective effort to govern.

The concept of deregulation rests heavily upon this vision of political actors. Because political action meets the needs of special interest groups and public officials, but not the needs of citizens in general, the effects of political action are undesirable from the perspective of any theory that favors individuals. Intrusions in the market are political action, of course, and are thus undesirable from this perspective.[53] But if the market is the ground condition, the presumption in the absence of market failure, efforts to create or preserve the market are not positive political actions. As a result, these efforts do not spring from the venal motivations that inspire regulation.[54]

To describe a political program as deregulatory is to characterize it as the undoing of positive actions, rather than as a positive action in itself. This program thus becomes associated with the innocence of nonintrusion. In restoring social organization to its natural state, the program escapes the sordid world of political self-interest. It seems to occur almost by gravity, and to be motivated more by remorse than by self-interest. But, in that

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51. *See, e.g.*, J. BUCHANAN & G. TULLOCK, *supra* note 47; D. MAYHEW, CONGRESS: THE ELECTORAL CONNECTION (1974); W. NISKANEN, BUREAUCRACY OF REPRESENTATIVE GOVERNMENT (1971); M. OLSON, THE LOGIC OF COLLECTIVE ACTION (1965).

52. For a public choice analysis that broadens the concept of interest groups, and advances an explanation for reregulation of that basis, see Weingast, *Regulation, Reregulation, and Deregulation: The Political Foundations of Agency Clientele Relationships*, 44 L. & CONTEMP. PROBS. 147 (1981).

53. For characteristic expressions, see D. ROBYN, BRAKING THE SPECIAL INTERESTS: TRUCKING DEREGULATION AND THE POLITICS OF POLICY REFORM (1987); A. STONE, *supra* note 37, at 171-95; THE POLITICAL ECONOMY OF DEREGULATION: INTEREST GROUPS IN THE REGULATORY PROCESS (R. Noll & B. Owen eds. 1983); Wilson, *The Politics of Regulation*, in THE POLITICS OF REGULATION (J. Wilson ed. 1980).

54. Cass Sunstein has suggested that the doctrine of substantive due process was based on a similar view that market allocations constitute a natural baseline against which government action must be judged. Sunstein, *Lochner's Legacy*, 87 COLUM. L. REV. 873 (1987).

case, reregulation constitutes positive action, a reassertion of the interest group dynamic that deregulation had escaped, and a return to the unnatural regulatory order that this dynamic spawns.

One difficulty with this view is that ordinary markets depend on the common law of contracts, a rather precise and consistently enforced set of legal rules. There are two notions, however, that can be invoked to absorb these rules into the natural order. The first is the assumption of social contract theory that contracts, and the rules of contract, are a naturally occurring phenomenon that preexists society, either historically or conceptually. The second is the view that common law in general is the way things simply are, an articulation of the natural order, rather than an identifiable set of governmental rules. Justice Holmes identified and attacked this view quite decisively,[55] but it has never really died, as Cass Sunstein[56] and Lawrence Tribe[57] have pointed out.[58] With both contract theory and the common law in general possessing these longstanding claims to naturalness, the use of contract law to enforce private agreements seems perfectly natural and unrelated to the mettlesome clan of regulatory programs.

Once again, economic analysis is linked closely to this political theory of action and nonaction. Just as economic analysis tells us that a free market maximizes wealth, it tells us that regulations which protect the market, or avoid disrupting it, will have a similar effect. Economic analysis thus adds a rather precise, normative argument to the image of political nonaction; these nonactions, which include deregulation and the common law, can be regarded as qualitatively different from other governmental policies because they tend to maximize wealth. In addition, maintaining a free market preserves the effectiveness of economics itself. To the extent that the free market is protected, modern economics can describe relationships within society, rather than simply providing an argument against those relationships, as it would in a regulated state.

The effort to extend economic models to political behavior provides further reason for favoring the free market. This effort depends upon the view that this behavior is a self-interested effort to maximize legislators' reelection, bureaucrats' power, and citizens' benefits. Any other behavior, such as the desire to secure the public good, simply cannot be modelled in economic terms. The economic analysis of political action thus tends to delegitimate that action by portraying its motives as venal. This does not quite explain why nonintrusion or deregulation is not similarly motivated,

55. *See, e.g.,* Southern Pac. Co. v. Jensen, 244 U.S. 205, 222 (1917) ("The common law is not a brooding omnipresence in the sky but the articulate voice of some sovereign . . . that can be identified."); *see also* Holmes, *The Path of the Law,* 10 HARV. L. REV. 457 (1897).

56. *See* Sunstein, *supra* note 51, at 883-902.

57. L. TRIBE, AMERICAN CONSTITUTIONAL LAW 561-81, 1711-15 (2d ed. 1988).

58. In a particularly striking affirmation, the United States Supreme Court held that passage of a statute did not constitute state action because the statute simply codified common law rights. Flag Bros. v Brooks, 436 U.S. 149 (1978).

but it will focus attention on the self-interested motives of any program that comes under scrutiny. If one assumes that economic theory already explains the market itself, and that the only remaining problem for the theory is to explain political intrusions, then scrutiny will be directed to those actions that alter the market, rather than the actions that maintain it. Thus, the desire for a comprehensive economic model tends to generate a concern with the self-interested motivations of the regulators and reregulators.

III. The Limits of the Deregulatory Vision

The natural market image that underlies deregulatory and reregulatory discourse, and its attendant views of individuals and politics, is not incorrect. It is simply preempirical; that is, it is generated by a vision of the world, not by empirical observation or logical proof. This vision may lead to desirable public policy in many circumstances, and we would be foolish to reject its implications. But the vision also has serious limitations, as do all such visions. To evaluate the concept of reregulation, one must recognize those limitations. In other words, one must get behind the framework which generates the term reregulation and think about the underlying image it implies. On that basis, an alternative image can be offered, and the two can be compared with respect to both their empirical validity and their normative appeal.

It is important to emphasize that this criticism of market and self-interest imagery is not intended as an argument that the market is the wrong social mechanism, that efficiency is the wrong social goal, or that economics is the wrong social science. The point, rather, is that these mechanisms, goals, and disciplines do not rest upon any objectively demonstrable foundations. Supporters must argue for the free market in the course of our ongoing debate about the proper way to organize our society, just as supporters of regulation, redistribution, or the use of sociology must argue for those mechanisms, goals, and disciplines. Very often, because the free market efficiency perspective is an appealing approach and is embedded in our cultural traditions, it will prevail. But it is simply a myth to transform these social choices into transcendent necessities.

A. Society

As an empirical matter, there can be little doubt that a free market, however "natural" it may seem to us, is not the usual manner in which social relations are organized. Studies of premodern societies have found varying amounts of market behavior, but they also find innumerable rituals, regulations, and traditions—a dense medium of rules, most of which bear little relationship to free exchange.[59] These rules are not an artifact of small,

59. *See, e.g.*, M. Douglas, Purity and Danger (1984); E. Durkheim, The Elementary Forms of the Religious Life (J. Swain trans. 1976); K. Polanyi, Primitive, Archaic and Modern Economies (1971); A. Van Gennep, The Rites of Passage (M. Vizedom & G. Caffe trans. 1961).

backward societies but a general feature of our social origins. When the curtain rises upon human history, it does not reveal unregulated communities, or communities taking their first hesitant, politically motivated steps toward regulation. Instead, it rises on a veritable science fiction world of comprehensive rules, public surveillance, state trading and manufacturing monopolies, and great masses of people marching in regimented teams to build vast structures with no instrumental function. Early civilizations were not unregulated or partially regulated cultures, but tightly organized islands, walled off from the surrounding chaos by an elaborate and intricate set of social regulations.[60]

In fact, it is difficult to find any society that maintained unregulated markets, or that included free exchange as an aspect of its ideology, until eighteenth-century Europe. Precisely why such markets and their attendant ideology developed at this time is far from clear. G. M. Trevelyan suggests that the Glorious Revolution, a conservative, rights-oriented reaction to the aleatory illegalities of the Stuart monarchy, generated a distrust of collective action and corporate institutions in the century which followed.[61] Combined with the Enlightenment mentality, and the first stirrings of the industrial revolution, this distrust produced an age of individualism and of governmental noninvolvement with private affairs. By the following century, it had been transformed into an ideology. While this ideology flourished in political discourse, it rapidly was abandoned as a practice—in Britain, during the latter half of the nineteenth century, and in the United States, during the first third of the twentieth.[62] The power of private citizens, which seemed familiar and benign when exercised by Britain's landed aristocrats or America's small entrepreneurs, became overwhelming and socially unacceptable when wielded by owners of vast industrial empires. So collective authority was reasserted: the state took responsibility for education, public health, housing, workplace conditions, workers' rights, and the maintenance of the poor. It was this new program that put the lie to Marx's dire predictions of class struggle, and insured the existence of capitalist democracies. Thus, the unregulated market represents a brief and bygone phase of human history, although it gave birth to an ideology that continues to the present day.

Nor does the free market seem to have any natural connection with industrial culture. While industrialization began during the laissez faire era, there were obviously innumerable other social factors at work, including

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60. *See* B. ALLCHIN & R. ALLCHIN, THE BIRTH OF INDIAN CIVILIZATION (1968); M. COE, THE MAYA (1971); J. MASON, THE ANCIENT CIVILIZATIONS OF PERU (1957). On the economic features of early civilizations, see TRADE AND MARKET IN THE EARLY EMPIRES (K. Polanyi, C. Arensberg & H. Pearson eds. 1957).

61. 3 G. M. TREVELYAN, HISTORY OF ENGLAND 11-15 (1926).

62. For Britain, see *id.* at 151-80, 232-52; *see also* A. BRIGGS, VICTORIAN PEOPLE 168-295 (1955). For the United States, see S. HAYS, THE RESPONSE TO INDUSTRIALISM 1885-1914 (1957); R. HOFSTADTER, THE AGE OF REFORM (1955); A. LINK, WOODROW WILSON AND THE PROGRESSIVE ERA (1954).

the growth of science, the Reformation, and European colonialism. Moreover, Russia and Japan have reached levels of economic development comparable to Western Europe and America by relying on state control, not laissez faire.[63] There has been much discussion about whether these nations would be better off with less centralized planning, and whether it is their successes or their failures that should be attributed to their collective actions. Nonetheless, their example serves any natural connection between industrialization and laissez faire, because no one can argue that Japan and the Soviet Union are not industrialized, and no one can argue that they are unregulated. Moreover, the non-Western countries that have industrialized most successfully in recent years—South Korea, Hong Kong, Singapore, and Taiwan—have followed the corporatist, regulatory model. This may be a feature of East Asian culture, to be sure, but that only supports the point: the approach to industrialization is a product of culture, not a natural process that transcends the social context. Thus, empirical evidence strongly suggests that the free market is a culturally specific phenomenon, rather than a natural form of human, or even industrial society.

There may appear to be something about the free market that differs from other social programs because it "just happened;" it was not the product of conscious social planning, like wealth redistribution. But, that position simply restates our cultural experience. The free market may seem natural to us, but monarchical authority seemed natural to our predecessors, government control seems natural to the Japanese, and theocratic rule seemed natural to Medieval Europe and the Maya. That which is embedded in one's culture always seems embedded in the nature of reality because culture constructs the reality that we perceive. The very dichotomy between autonomous occurrence and conscious planning, which lies at the base of the entire claim, is cultural; we perceive the distinction, and attach significance to it because that is our experience.

The market is not quite as autonomous as it appears, even within our cultural context. It depends upon a rather specific set of social rules and programs, most notably the enforcement of private contracts and the centralized control of money. We tend to ignore the programmatic aspect of contractual rules because they were developed by decentralized decision-makers, and emerged from a dispute resolution process, rather than being the product of conscious, centrally created social policy. But all this naturalness is an illusion; the enforcement of private contracts seems natural to us because it is ours. Placing power in the hands of lawyers and judges, rather than bureaucrats, may be an unusual way to govern a society, but few outsiders would fail to perceive it as a form of governance. With respect to money, even the decentralized feature of government regulation

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63. For the role of central planning in these countries, see O. IOFFE, THE SOVIET ECONOMIC SYSTEM: A LEGAL ANALYSIS (1987); C. JOHNSON, MITI AND THE JAPANESE ECONOMIC MIRACLE (1982); LAW AND ECONOMIC DEVELOPMENT IN THE SOVIET UNION (P. Maggs, G. Smith & G. Ginsburg eds. 1982).

disappears. Money supplies have been regulated by some executive agency through most of the free market era.[64] At present, all major industrial nations rely upon a highly administered mechanism—totally symbolic currency, issued against the general credit of the government, and controlled by its central bank. Again, the free market is simply a social choice for a particular kind of regulation, not only in its negative features of nonintrusion upon private agreement, but in its positive features of enforcing those agreements, and creating the money with which they are transacted.[65]

B. *Individuals*

The vision of individuals that is derived from the free market image, and thus underlies deregulation and reregulation discourse, is no less culturally specific than the market image itself. As an empirical matter, societies simply do not consist of autonomous individuals with independent preferences based on their own self-interest. Both the phylogeny and ontogeny of cultural experience suggests that there exists a complex interaction between individuals and their society, and that this interaction creates individuals as we know them. In terms of social phylogeny, the contract theory is obviously not a real anthropological account; people do not exist outside of culture, nor do they have a set of recognizable independent values apart from their cultural context. Rather, culture constructs the individual by defining interests, generating preferences, and establishing a system of symbolic rewards, material allocations, and power relationships through which those interests and preferences are expressed. Social ontogeny recapitulates this process. Our individual experience is not one of standing outside our culture and deciding whether it meets our desires. Rather, we are "thrown" into a social context long before we are able to make critical evaluations, or even able to think of ourselves as selves.[66] By the time we are ready to make any significant individual choices, we speak, act, and think in culturally constructed ways.

In virtually every society, of course, individuals are able to separate themselves from their established roles, to perceive a field of action that ranges well beyond the limits of social approval, and, in some cases, to act on their perceptions. To conclude, however, that these thoughts and actions transcend the cultural context and reveal a preexisting set of preferences oversimplifies the concept of a culture. Cultures do not consist exclusively of rigorously defined roles, but create a complex, ever-changing set of roles and meanings. They contain within themselves the possibility of dissent, transformation, violation of social norms, and self-aggrandizement at the

64. Adam Smith recognized this necessity for regulation of money. *See* A. SMITH, THE WEALTH OF NATIONS 304-08 (1937 ed.).

65. For a description of monetary control in the United States, see S. MAISEL, MANAGING THE DOLLAR (1973); T. MAYER, J. DUESENBERRY & R. ALIBER, MONEY, BANKING AND THE ECONOMY (2d ed. 1984).

66. M. HEIDEGGER, BEING AND TIME (J. Macquarrie & E. Robinson trans. 1962).

expense of existing traditions. But all of these actions are structured by culture, and played out in a culturally constructed arena. Most societies experience dissent, for example, but the character and meaning of that dissent is as variable and as contextual as the traditions it opposes.

We may feel intuitively certain that we, as individuals, are motivated by autonomous, self-interested behavior, and that our society is structured in response to motivations of that sort. But in this instance, our intuitions and our observations of ourselves and of our society constitute a rather unreliable datum. Autonomous, self-interested behavior is our own cultural norm. This behavior provides our dominant theory for justifying our political regime, and a working set of motivations for our economic markets. Clearly, we do not believe in and practice this behavior in opposition to our culture; we do so because it is our culture, because our culture constructs us in this way. This argument can be carried too far, of course, as one can describe every theory or belief as culturally specific. But in this case, the imagery of markets and autonomous individuals is so clearly a cultural perspective that we cannot accept our own intuitions about the subject as evidence of a transcultural phenomenon.

C. Politics

The role of culture and society undercuts any theory of politics or of the state that is derived from the free market image. Since there is no evidence to support the view that the market is a natural form of social organization, and there is no evidence to support the view that individuals are anterior to society, there is no reason to assume that the polity is best conceived as a contractual alliance among natural antagonists. Rather, society and individuals interact as part of a collectivity. Given that interaction, the social structure must be understood as a collective choice, to the extent that it constitutes a choice at all. We do not begin as autonomous individuals who choose a social structure; we begin as members of a social structure, whose range of decisions is defined in relation to that structure. The initial question, therefore, is not what kind of society we want to create, but how we change or preserve the society in which we exist. This clearly applies to our own particular social contract myth. We speak of the Constitution as a contract among individuals, but, even apart from its historical antecedents like the Articles of Confederation or the state constitutions, the Constitution clearly was adopted through an existing institutional structure, and by a group of people who possessed a preexisting sense of themselves as a decisionmaking collectivity.

Turning to practical, contemporary politics, the same conclusion emerges. The modern state clearly has the power to displace any social structure, like the market, that seems to respond to individual preferences. That power, of course, is precisely what leads many market-oriented thinkers to be highly distrustful of collective action. In doing so, however, these thinkers acknowledge the primacy of the collectivity; their arguments are generally directed to that collectivity because that is where decisions must be made.

Of course, those decisions might well empower individuals to express certain preferences through the market, as these thinkers recommend. But the desirability of such an approach is necessarily a matter for debate, a debate carried out in a collective, political context.

There is nothing in the nature of that debate to suggest that market solutions should be preferred *a priori* to other alternatives. The only thing that distinguishes the market from any other social policy is the belief that the market is a natural form of social organization. Once we part with that belief, the market simply becomes one option that fulfills some purposes and frustrates others. Maintaining or restoring the free market becomes an ordinary political decision, subject to the same public choice phenomena as any other. Some legislators want to regulate the market to appeal to powerful interest groups; others want to preserve the market in order to appeal to different, equally powerful interest groups. There being no saints in sight, our only choice is between rival sinners.

Thus, deregulation cannot be viewed as a miraculous release from interest group pressure or as the sudden result of society coming to its senses. In fact, a wide variety of interest groups are aligned on the side of deregulation. With respect to the financial services industry, every industry group has championed deregulation of the other guy's business and preservation of its own. Securities firms have been delighted to see deposit services deregulated, but have fought the deregulation of underwriting with savage ferocity; large banks have been insistent that the deregulation of underwriting is central to our national well-being but are determined to deny other financial institutions access to deposit insurance or to the payment system. This debate has proceeded as a struggle among these various groups, not as an effort to restore the natural order.

IV. THE POSSIBILITY OF ALTERNATIVE VISIONS

A. Policy

The terms we use reflect and in many cases alter the way we conceptualize our policy debates. With respect to the financial services industry, most people characterize the elimination of interest rate restrictions, the abandonment of geographic barriers to interstate banking, and the increasing overlap in products among various financial services firms as a process of deregulation. The consumer legislation involving creditor practices, credit extension, funds availability, and payments generally might then be seen as a reregulatory initiative.

As suggested above, this is not a particularly illuminating way to view these events. The market imagery that stands behind the terms "deregulation" and "regulation" is no better than a "Whig" interpretation.[67] By taking the free market as a natural starting point and autonomous self-

67. H. BUTTERFIELD, THE WHIG INTERPRETATION OF HISTORY (1965).

interest as a universal pattern of behavior by both market participants and public officials, the market interpretation of history obscures the complex interplay of values and strategies. It suggests that every act of regulation is a triumph of special interest groups at the expense of citizens in general, or a grim necessity in the face of market failure. This market interpretation of history also suggests that every act of regulation in the wake of a deregulatory movement is reregulation, where special interests or grim necessity reassert themselves. Human progress, according to this view, is measured by the freedom of the market and its restoration following the regulatory night.

In fact, there is no such teleology; instead, as Arthur Okun suggests,[68] there is an ongoing contest between the market-oriented policy of economic efficiency and such other values as redistribution, social stability, or consumer protection. Each strategy that emerges from this normative stew needs to be evaluated in its own right and within its own context, not against a fixed background formed by one of these contested values. The more useful perspective, therefore, is that the recent events in the financial services industry involve rival visions of the industry in question. As a society, a collectivity, we must choose among these rival visions. There is no natural ground plane to fall back upon; every policy represents a choice, a choice that is necessarily being made by the collective processes that govern our society.[69]

The great difficulty is that we have no coherent way to choose among social policies. We know how to carry on the debate, and we do so with considerable enthusiasm, as the history of the financial services industry suggests. Moreover, the results that emerge are often perfectly respectable, reflecting the Anglo-American talent for practical politics. Nonetheless, it is irritating to lack any conceptually satisfying methodology for structuring and resolving such debates. The siren song of economics and efficiency is that they provide such a methodology; if we demote them to being one of several disciplines and policies, we lose the sense of certainty with which they beckon us.

Jurgen Habermas suggests that we can never develop a methodology for choosing among social policies, that there will never be persuasive rules for structuring or closing off our normative debates.[70] Instead, he proposes a continuing dialogue, with formal rules about the kinds of arguments that can be advanced. This is certainly a useful antidote to positivism, which is Habermas' *bete noir,* but like many critiques, it bears the imprint of its target. Habermas seems overly optimistic about our ability to develop fixed and finally persuasive rules to govern our normative debates. These debates proceed not only by abstract, reasoned argument, which is Habermas'

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68. A. Okun, Equality and Efficiency: The Big Tradeoff (1975).

69. For discussions of regulation at this level, see The Limits of Government Regulation (J. Gatti ed. 1981); Rights and Regulation (T. Machan & M. Johnson eds. 1983).

70. J. Habermas, The Theory of Communicative Action (T. McCarthy trans. 1983).

choice, but also through social institutions, political action, and public opinion.[71] In the financial services field, for example, the rapid development of consumer protection laws resulted largely from the consumer movement's ability to organize and to function effectively as a political lobby and a social force. This was not simply because the consumer movement could threaten legislators with electoral punishment. Rather, the public policy arguments advanced on behalf of consumers would not be understood, would not be perceived by the intuitive process that dominates politics, without an organizational structure to argue in their favor.

All this may seem rather pessimistic. Not only is there no definitive methodology for designing social policy, as proponents of economic analysis promise, but there is no definitive way to structure our policy debates, as Habermas and other critics of such methodologies suggest. But this sense of pessimism is itself a social construct, a reflection of our unrealistic expectation that some ground of certainty exists to resolve our present quandaries. A more reasonable expectation is that we can develop a variety of devices to improve the ongoing process in which we are engaged. These devices can be discoursive, technical, or pragmatic, as Donald McCloskey suggests;[72] they could operate at any of the levels at which our normative debates are conducted.

One such device is a recognition of the belief systems implicit in our choice of terms, and an explicit evaluation of those belief systems. As suggested here, the terms deregulation and reregulation carry with them a rather elaborate image of a free market as an ideal form of social organization. That image is neither wrong nor reprehensible, but its claim to universal truth is eminently debatable. Structuring our discourse according to these terms obscures the contours of the debate, burying its controversial elements at a depth where the opposing sides can react only with affirmation or annoyance, rather than reflective evaluation. Those who favor "deregulation" tend to feel astonishment that anyone would fail to perceive the inefficiency and undesirability of regulation. Those who welcome "reregulation" regard their opponents as morally insensitive to the miseries and rigors of the market. But these positions get us nowhere. If we perceive, instead, the two groups as proposing rival public policies, we can more readily evaluate each alternative, even if we must do so without the benefit of a synthesizing methodology. We then have the option of recognizing that they each may address different social problems on different aspects of an issue, and we can avoid being drawn into global affirmations or dismissals.

This alternative approach to social policy debates implies a less heroic, but more realistic role for scholars. No scholar will ever find the key to social policy, the method of analysis which demonstrates decisively that one policy is correct, and all the others wrong. There is no such key. What

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71. For a description of public opinion on these matters, see S. Lipset & W. Schneider, The Confidence Gap 221-56 (1983).

72. *See* D. McCloskey, *supra* note 43, at 36-46.

scholarship provides is a way to understand the policies that lie behind our institutions and instrumental strategies, or the institutions and strategies that our policies imply. Such clarifications and elaborations do not constitute the entirety of legitimate social policy debate, but they represent one of its more significant components.

B. Economics

A second device for improving our process of social decisionmaking is the use of technical knowledge. In the case of financial services, the body of knowledge that comes most naturally to mind is, of course, economics. But economics, like scholarship in general, cannot function as a means of resolving the debate about alternatives; it serves as a comprehensive methodology for evaluating social policies only if one has already resolved the debate in favor of a policy of wealth maximization, or efficiency. Although this is widely recognized, some economists and law and economic scholars have overstated their case by trying to demonstrate that efficiency is an objectively desirable goal. Once economics has been manacled to efficiency in this way by its friends, the two are readily exiled together by their enemies.

Deregulatory discourse only deepens the confusion. Because it is based on a preempirical and preconceptual image of the market, deregulation is more difficult to domesticate than the connection between economics and efficiency. Deregulation suggests that there is no other useful way to approach social issues because markets, autonomous self-interest, and a polity of antagonistic individuals are part of reality, the way things really are. Because economics can model these phenomena, the discourse suggests that economics is a natural method of analysis. And because economics indicates that these naturally occurring markets are efficient, the discourse suggests that efficiency is a naturally occurring social policy.

In fact, none of these links are necessary ones. The ability of economics to model unregulated markets, and its conclusions that such markets are efficient, is only one function of this discipline. Economics also is capable of dealing with phenomena outside unregulated markets, and it can be utilized for many social policies besides efficiency. In the case of individuals, economists long have acknowledged that they cannot explain the origin of human preferences, nor can they make definitive comparisons between one person's preferences and another's. What they can do is to predict market phenomena that respond to preexisting human preferences. In other words, given individual desires and some other data, economists can predict the price. The same is true for society at large. Economics cannot tell us how to choose between rival social policies, for that depends upon the social preferences that emerge from our political process. In some cases, we want efficiency; in other cases, we want redistribution, consumer protection, or stability.

But economics can indicate the prices of these other policies. Such social prices are more difficult to model mathematically, but even at a lesser level of precision, economic analysis provides useful information. The fact that consumer protection, for example, can only be achieved at a given social cost does not prove that this policy is undesirable, any more than the higher price of a scarce good can prove to an individual that the good should not be bought. But it is certainly helpful to know the price before purchasing the policy. Furthermore, economics often can tell us how a particular policy can be achieved at the lowest possible price. One strategy for protecting consumers may impose high costs by disrupting markets, while another may achieve the same level of protection with less disruption and less cost. Such intrapolicy comparisons, like intrapersonal or ordinal comparisons of preferences, are more defensible than the interpolicy variety. It is virtually unarguable, for practical purposes, that we should prefer to achieve our chosen goal at a lower price, rather than at higher one.

Such uses of economics must be distinguished from a market failure argument. Market failure is an aspect of efficiency analysis, since a market that fails is one that cannot achieve efficient results without some form of corrective intervention. Even so, the law and economics movement has not been particularly enthusiastic about exploring alternative modes of intervention; the preferred approach seems to be a Herculean effort to explain away the apparent market failure so that no intervention is necessary. This instinct springs from the preempirical norm that the market is natural and desirable per se. But there is certainly nothing in a market failure analysis that conflicts with a policy of economic efficiency or with a comprehensive economic analysis. The argument based on alternative policies is different. It does not claim that the market has failed in a particular area, but that a market is not the social policy that we should employ to achieve our objectives. While economic analysis can still be used in designing such a policy, it must clearly be subordinate to other considerations.

There is a tendency to conflate the distinction between market failure arguments and social policies that aim at objectives other than efficiency. Market-oriented scholars who recognize the value of alternative policies may try to absorb these alternatives into their economic framework by presenting these policies as solutions for market failure.[73] This locates the alternative policies within a general context of efficiency and treats them as secondary modifications of the efficiency analysis. In some cases, this conflation of separate arguments may serve a social purpose by building a provisional consensus between rival groups. The scholar's role, however, is to think clearly about these matters, to disentangle the interwoven strands so that we can evaluate the advantages and disadvantages of various social policy alternatives, and the value of reweaving them.

CONCLUSION

The terms "deregulation" and "regulation:" have an *au courante* crackle to them, but they spring from a rather dusty system of free market

73. *See supra* note 39 (citing sources).

imagery that has been with us for some time. This system, partly normative and partly conceptual, makes distinct assertions about social organization, human behavior, and political action. By using deregulation-regulation discourse, we place ourselves amidst this imagery, and thus take its assertions for granted. We assume that the discourse is telling us about the nature of society, human beings, and politics, when it is really telling us about itself. This does not mean that the imagery produces bad results; it simply means that it is imagery. Those who want us to adopt this imagery must present arguments in its favor, not unprovable declarations of its inevitability. They must give us a reason why we should think of our society and ourselves in these terms rather than in others.

As it turns out, there are some rather powerful arguments for doing so. Free market imagery generates a social system that allows us to achieve economic or material efficiency. That is an appealing goal, and it is especially appealing in a commercial area like the financial services industry. In addition, this imagery permits us to use economics, the most precise of our social sciences, as a comprehensive methodology for solving social problems. The power of economics should not be underestimated, particularly when its practitioners adopt a responsive, nontendentious attitude toward market failure. Many of the consumer issues in the financial services industry, for example, can fully be described and analyzed in purely economic terms.

But the appeal of efficiency and the power of economics should be used to enlighten, not to dazzle. Efficiency is only one of many social policies. Public debate often runs various policies together, probably to our great advantage, but when the strands are disentangled, there is no evidence that society is prepared to opt for efficiency to the exclusion of all other choices. Scholars, whose job it is to trace the separate strands, cannot prove that efficiency is the only valid one. Economics, however readily it meshes with efficiency, has many other uses. It can serve other policies as well, although none of the others will grant it the seductive sense of centrality that material or economic efficiency confers upon it.