Accommodating Power: The “Common Sense” of Regulators

Forthcoming, *Social and Legal Studies* 18(2), 2008.

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April 19, 2008
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7526 Words

*This paper has benefited from the generously shared legal insights of Professor Joan Brockman (Criminology, Simon Fraser University), and from the incisive critiques of Professors SteveTombs (Johns Moore University, Liverpool), and James Williams (Sociology, York University). I am also deeply indebted to the regulatory and IMET officials interviewed, who gave their time and shared their insights.

Abstract:

The paper examines the perspectives, strategies and practical "common sense" of those charged with regulating and enforcing securities laws in the post-Enron era. It is an empirical study of stasis and fluctuation, of *habitus,* the practical/common sense regulators acquire, practice and live (Bourdieu, 1987, 1993), and its continual fine-tuning. Using 21 interviews with regulators and enforcement staff in securities commissions and law enforcement, and key regulatory documents (legislation, commissioned research reports, in-house policy directives), the paper shows how officials negotiate their regulatory terrain and accommodate the economic and social capital of the powerful financial players they regulate, *and* how they re-situate their mission as ideological currents change. Two interconnected arguments are made: first, the compliance-oriented rationale that guides the day-to-day activities of the regulatory agency constitutes, reinforces and reproduces the asymmetric power relations of its operational field; that is, agencies have institutionalized, and securities regulators have interiorized certain structurally mandated realities of the relations of power they operate within. Second, the *habitus* thus formed is constantly responding to alterations in the regulatory field. Thus crackdown periods following stock market disasters empower regulators – particularly staff charged with prosecuting and sanctioning offenders –to act on the always simmering internal contradictions between the compliance mission of the agency overall and the enforcement missions of Enforcement/Litigation branches.

Key Words:
Corporate Crime, Regulation, Stock Market Fraud, Governance, *Habitus*

> "*A system of governance is most effective when governed subjects voluntarily adopt and internalize its norms, values and ambitions as their own"*
>
> Rose, 1989: 50

> *The OSC seems not to have been captured by the sector it regulates but handed over to them"*
>
> Andrews, 2006: 86

Introduction:

The paper examines the perspectives, strategies and practical "common sense" of those charged with regulating and enforcing securities laws in the post-Enron era. It is an empirical study of stasis and fluctuation, of *habitus,* the practical/common sense regulators acquire, practice and live (Bourdieu, 1987, 1993), and its fine-tuning. Using 21 interviews with regulators and enforcement staff in securities commissions and law enforcement, and key regulatory documents (legislation, commissioned research reports, in-house policy directives), the paper shows how officials negotiate their regulatory terrain, both accommodating the economic and social capital of the powerful financial players they regulate, and re-situating their mission as ideological currents change. Two interconnected arguments are made: first, the compliance-oriented rationale that guides the day-to-day activities of the regulatory agency constitutes, reinforces and reproduces the asymmetric power relations of its operational field; that is, agencies have institutionalized, and securities regulators have interiorized certain structurally mandated realities of the relations of power they operate within. Second, the *habitus* thus formed is constantly responding to alterations in the regulatory field. Thus crackdown periods following stock market disasters empower regulators – particularly staff charged with prosecuting and sanctioning offenders –to act on the always simmering internal contradictions between the compliance mission of the agency overall and the enforcement missions of Enforcement/Litigation branches. At these junctures agencies receive a short-lived cultural permission to pro-actively scrutinize the practices of dominant economic actors.

In 1992 Nancy Reichman pointed out that business actors exercise power in ways blue collar criminals do not, through their ability to influence the form, shape and meaning of regulatory law. Enforcement policy, she argued, emerges from the "informal arrangements, tacit agreements and pressures for conformity" exercised by "complex networks of clients, legal and accounting personnel and market competitors" (Reichman, 1992:245). The corporate sector, through its political, social, ideological and economic capital, is thus legitimized as an inside player with the cultural authority to shape the meaning and interpretation of formal regulatory law. Putting empirical clothes on these claims, Mary Condon's 1998 study of stock market regulation in Ontario from 1945-1990 showed how key business players used their cultural capital and inside player status to shape securities legislation. Recent work has further documented the innovative strategies corporate actors devise to stretch legislative controls further still (McBarnet, 2004, 2006). Thus as each newly discovered financial disaster generates another flurry of reform

legislation, corporate lawyers, accountants, consultants and bankers begin devising new ways to shape, stretch and legally circumvent it. "Screwing the (financial regulatory) system" is culturally celebrated and *very* lucrative.

This paper examines the formative role played by the targets of regulation in constituting the regulatory terrain (see Haines & Sutton, 2003; Parker, 2006). Following Bourdieu, it argues that the *habitus* of regulators - the strategies and techniques, the formal arrangements and informal expectations regulators employ - is produced by "the dialectical interplay between incorporating … objective features of the organization of social fields" and "externalizing… this through… the subject's reproductive labour" (Bourdieu, 1993: 54). As regulators and regulated populations create and reproduce "the structural conditions of [their] social fields", this process of internalization generates the mentalities, sensibilities and practices of both groups (Frauley 2005: 181-5). Becoming a successful regulator is all about incorporating these structurally generated, taken-for-granted realities of business/government interaction. But while the frame of the regulatory field is relatively constant, its boundaries are constantly re-negotiated in response to a myriad of global, national and regional events (Gunningham, Kagan & Thornton, 2003; Gunningham & Johnstone, 1999; Hutter & Jones, 2006; Haines, 2003; Parker, 2002). Crackdown periods following major financial disasters – here, the collapse of the technology fuelled stock market bubble in 2000/2001 – shift the balance of power between agencies and business in a pro-regulatory direction.

Stock market regulation in Canada, the empirical focus of this paper, illustrates another set of influences, showing how local/regional intersect with global/universal forces to shape regulatory terrain. Canada's resource-based economy (mining, forests and oil), its history of French/English compromise (native peoples always excluded), and its federal-provincial struggles have produced several unique features. Canada is the only developed nation-state without a national stock market regulator, power is fragmented across 13 jurisdictions and securities commissions (Phelps et al, 2003). Rivalry is particularly fierce between the pre-eminent commissions in Ontario, Quebec, Alberta and British Columbia. Canada's regulatory environment is distinctly bimodal: most public companies are small, but the few major multinationals, primarily located in Ontario, typically dual-listed and therefore dual-regulated, dominate the financial landscape (Nicholls 2006). But large issuers comprise only 10% of the 3000 plus companies listed on the 13 Canadian exchanges (Nicholls, 2006: 135).[1] Nationally, 40% of companies offering shares are worth less than $10 million (Sibold, 2005), family ownership and concentrated control are common.[2] However Canada's economic, political and cultural dependence on the world's pre-eminent superpower, the United States, is a feature shared today by most of the developed world. Canada has the largest number of non-American companies listed on the US-based Securities and Exchange Commission (497 of 1240 foreign companies as of January 1, 2005).

Section I of the paper presents a mini-genealogy on the origins of regulation and their significance today. Section II outlines the latest stock market crisis, the "crackdown" and its regulatory legacy. III presents the empirical findings from interviews and document

analysis. The final Section links the empirical to the theoretical, showing stasis and fluctuation, constancy and change.

Section 1: Origins

Two centuries ago, the basic principles of stock markets - dispersed ownership and publicly sold shares through the vehicle of the corporation - were heavily contested. Incorporation was a privilege granted by the nation-state in exchange for services and/or cash (Glasbeek, 2002; Snider, 1993). Adam Smith, the very father of capitalism, warned against separating ownership from control, arguing that incorporation should only be allowed for "exceptional economic undertakings", where the discretion of management is "so limited that it cannot help but coincide with the investors' interest" (Glasbeek, 2002: 72, from Smith, 1994; also Berle and Means, 1932). Stock trading was viewed as ungentlemanly, the "free" market was similarly suspect (Shearing, 1993). Every major precept - the "common sense" of the financial domain today – had to be conceptualized, argued as a problem-solving solution by the authorities of the day, and legitimated through business schools, think tanks and select public media (for example, *The Wall Street Journal)* (Shearing, 1993; Garland, 2001; Pearce & Tombs, 1998; Snider, 2004).

By the dawn of the 20th Century this ideological task was done, and finance capitalism began its meteoric ascent to hegemonic dominance. Government regulation was developed reluctantly, to tackle two conflicting realities: "nation-building" could only be achieved by raising capital and developing Canada's natural resources, but the industries involved, particularly mining, showed a lamentable, repeated susceptibility to fraud, threatening investor confidence and therefore nation-building. Thus 13 regionally based regulatory agencies were established. The Ontario Securities Commission, the largest and most powerful, was established in 1928 to oversee the Toronto Stock Exchange (TSE, now TSX), and the Broker Dealers Association (BDA)[3] (Stenning et al, 1990; Condon, 1998: 19-20).

The legacy of this is a regulatory system rooted in a shared set of assumptions marked, first, by "an essential faith in capitalism so obvious it goes … unrecognized" (Stenning et al, 1990: 12). "Common sense" then and now holds that everyone has the God-given right to strike it rich by pouring money into a piece of hinterland moose pasture – and good on her if she can persuade a dozen chums to do the same. Selling stocks to raise money for capital pursuits is intrinsically a "good thing", an activity to be rewarded and facilitated. Therefore formal or criminal law was always a last resort, useful only after "broad discretion", and "courts of honour" have been tried and failed (Andrews, 2006: 71). This is reflected in the contradictory goals of regulation– to promote *and* to sanction risk-taking. These subterranean "first principles" exert constant ideological pressure on agencies to justify every statute and sanction, and they reinforce the cultural permission of business to shape and resist regulation.

Section II: The (Latest) Regulatory Crackdown[4]

The bursting of the stock market "bubble" in 2000/01 revealed systemic, routinized corporate fraud. It produced state-sponsored "crackdowns" in law, professions, standard-setting organizations and SROs (Self-Regulatory Organizations). In the United States, the pivotal Sarbanes-Oxley Act (SOX) of 2002 increased reporting requirements, penalties and oversight over audits, financial reports, corporate counsel, senior executives and Boards of Directors.

Historically, efforts to govern corporate crime have been cyclical, with each corporate disaster bequeathing a "regulatory legacy" (Haines & Sutton, 2003). Mine explosions (Glasbeek, 2002), factory fires (Haines, 2003), chemical leaks (Pearce & Tombs, 1998), oil spills, and the now-forgotten collapse of the S & Ls in deregulated 1980s America (Calavita et al, 1997) all motivated "get tough" rhetoric and law. Typically, deregulated statutes are revived, regulatory agency budgets increase, regulation-as-government-interference rhetoric declines. Alas, when media spotlights shift, agencies retreat, budgets are savaged[5]. Tax lawyers and accountants quickly institutionalize new ways to evade, avoid or nullify the latest set of regulations (McBarnet, 2004, Braithwaite, 2005) - until the next crisis (Rosoff et al, 2006; Calavita et al, 1997; Snider, 1993). This has produced "juridification", a jumble of complex, contradictory rules (Haines, 2006).

Loss of investor confidence and the passage of SOX shaped the regulatory response in Canada (Nicholls, 2005:139). Regional rivalries necessitated federal policies crafted to suit the specificities of Canadian markets while not exacerbating provincial rivalries. In 2003 the federal government authorized the national police force, the RCMP, to establish Integrated Market Enforcement Teams (IMET) to "detect, investigate and prevent" serious capital market fraud (www.rcmp.grc.ca). Each multidisciplinary unit had specialists in accounting, economics and law enforcement. IMET was championed by John Sliter, a senior RCMP officer who realized the Enron-induced atmosphere of crisis provided the necessary window of opportunity. As he put it: "the government was desperate" (Interview, May 2006). On February 12, 2004 Bill C-13[6] criminalized "improper insider trading" (maximum penalty 10 years), doubled penalties for "market manipulation" (section 382), and created the offence of "tipping", "knowingly convey[ing] inside information …. to another person, knowing [they might] use the information to buy or sell, directly or indirectly, a security ….. " (section 382.1(2) *Criminal Code)*. (Unless specified, fines under the Criminal Code are unlimited.) This legislation also introduced Production Orders compelling banks and other 3rd parties to provide "all necessary documents" (section 487.012), whistleblower protection (section 425.1 (1)), and sentencing guidelines spelling out "aggravating factors" to toughen penalties (section 380.1 (1) *Criminal Code)*.[7] Lenience was deemed problematic because: "weak and inconsistent enforcement [threatens] investor protection… [making] adjudication "costly, duplicative .. inefficient and unduly delayed" (Phelps et al, 2003: 25). To soothe provincial sensibilities the federal government promised its authority would be restricted to cases that "threaten the national interest in the integrity of capital markets" (Mackay & Smith, 2004: 2).

Bill C-13 and IMET were designed to counter accusations of "lenience" and bring stock market regulation in line with regulatory and ideological shifts in the United States. Non-

governmental self-regulatory and standard-setting bodies responded similarly. The Toronto Stock Exchange, the Investment Dealers Association, and the Canadian Venture Exchange (now the TSX Venture Exchange) issued guidelines "urging" security analysts and mutual fund dealers to adopt new conflict of interest rules. The Canadian Bar Association tightened ethics rules for corporate counsel (Paton, 2006). The Canadian Coalition for Good Governance, formed in June, 2002, recommended measures "to provide more power, oversight and independence to boards of directors and audit committees". In 2005 Ontario amended the Securities Act to facilitate investor suits in hopes of activating a civil law deterrent (Glendinning and Blair, 2006).

However backlash, the predictable retreat from regulation, is growing fast. In the United States, critics label Sarbanes-Oxley "excessive and ill-conceived", alleging that the "burden" of regulation is killing Wall Street (*Globe & Mail,* January 2, 2007: B5). The reform-minded William Donaldson, appointed Chair of the SEC in 2002, has been replaced by Christopher Cox, a Wall Street insider more sympathetic to industry concerns. Industry lawyers are preparing lawsuits to declare SOX unconstitutional; the U.S. Chamber of Commerce and Wall Street-sponsored task forces have listed measures for elimination. Auditing rules requiring public companies to certify their internal financial controls – the very provisions that forced 8 percent of all listed companies in 2005 to "restate" their earnings - have been modified. Christopher Cox has asked the Independent Public Company Accounting Oversight Board (a pivotal SOX-mandated agency) to "revise" its auditing rules to "lessen the auditing burden". And the U.S. Justice Department is presently passing guidelines to limit the powers of prosecutors to lay charges (Sources: *Globe & Mail,* January 2, 2007: B5; *International Herald Tribune,* 2006, accessed online November 15, 2006; *New York Times,* April 8, 2007).

In Canada, the Ontario Securities Commission has replaced its entire management team, importing 2 former bank executives as Chair and Executive Director, and 2 securities lawyers as Vice-Chairs. And it is "rethinking" its enforcement strategies after a high profile insider trading case was overturned on appeal. According to its Vice-Chair, "it may be that you just cannot get insider trading convictions in a criminal court" because "the standard of proof is so high" (*Globe & Mail,* April 9, 2007: B2). If this retreat continues, the threat of incarceration, a seldom-used but significant denunciatory symbol and deterrent, will disappear (Braithwaite 1989). As several regulators interviewed for this study put it: "the pendulum is now swinging back"; 'there's the belief .. that Enron measures went too far' (Interview January 2006).

And IMET, launched with great fanfare and high expectations 5 years ago, has still laid no charges in any of its high-profile cases.[8] IMET's most public venture was a raid at the headquarters of the Bank of Nova Scotia[9] on Bay Street (Canada's Wall Street) at the height of rush hour. Officers in 3 brightly marked police vans removed box after box of documents. This raid, front page news in all major media, provoked outrage and vicious media attacks, vilifying IMET for both "over-reacting" and "under-reacting" to business crime – that is, for laying charges on insufficient evidence *and* for failing to lay criminal charges. "The RCMP's IMET has little to show for itself", a lead editorial in the *Globe & Mail* trumpeted on May 22, 2006 (A12); and "RCMP's IMET hit by senior staff

defection; no charges yet laid in prominent cases" (*Globe & Mail Report on Business,* March 16, 2006: B1, B7).

Section III: Regulators' Perspectives

This study is based on 21 interviews with Commissioners, Directors and Assistant Directors and staff in the Ontario Securities Commission in Toronto and the British Columbia Securities Commission in Vancouver. Additional interviews were conducted with IMET officers and staff in Vancouver, Toronto and Ottawa, and with one official from the Department of Justice, the ministry responsible for Bill C-13. While securities commissions and IMET operate under different legislative regimes and governments (provincial vs federal), their missions – to protect market sanctity and reinforce investor confidence – are similar. Interviews, done by the author from January to June, 2006, lasted from 65 to 120 minutes (average length 90 minutes). To maximize spontaneity and confidentiality they were not taped. Detailed notes were taken during the interview, intensive summaries were recorded immediately after it. Interviews were semi-structured, allowing respondents to concentrate on issues they saw as significant. In addition, a wide range of documents– Staff Notices, Policy Guidelines, Royal Commission Reports, enabling legislation and Parliamentary minutes - were reviewed.

1. Compliance: The Dominant Rationale

True to its origins, the central rationale of stock market regulation, expressed in mission statements and legislation, is to foster investor confidence by ensuring compliance with regulatory law. Promoting and achieving compliance is parcelled out to divisions or branches, typically labelled Community Relations, Compliance, Prevention and Enforcement/Litigation. Their primary task is to secure compliance, whether through education, communication, monitoring, or sanctions.

Thus interviewees, from senior executives down, emphasized the importance of educating business. Officers noted that much of their time is devoted to offering businesses advice on "good business practices" that facilitate compliance, and on cultivating relations of trust with business. Staff regularly consult business (their officially designated "stakeholders") for feedback and advice, and solicit business opinions on prospective policy changes. "The goal of our actions is to create [a] level playing field [so that] all follow the same rules –protection of public and don't lie to the regulator! … Sometimes they omit stuff, but we have to have basic trust relationships."[10] (January 2006). Note his use of the word "omit" rather than "hide".

Creating and sustaining good relationships was prioritized: "Good faith and respect for the industry are our starting points. This is adjusted only by experience." The regulators' operating philosophy is "start with trust and escalate only 'for cause'. All officials stressed the good faith of the business community overall: "Over 90% are trying to do a good job", and the importance of regular consultation with "stakeholders' to ensure "we are on the same page". Regulators stressed their unceasing efforts to avoid "over-regulation" – no one spoke of "under-regulation". Staff at all levels mentioned their

attempts to speed up the review and approval process, “cut the regulatory burden” and reduce “the costs of compliance” (all from Interviews, January 2006).

This does not mean officers were naïve about business motives for compliance. They believed businesses obey regulations because they fear loss of reputation and economic losses, not out of ethical conviction. Indeed respondents pointed out that this was the greatest impact of the latest crackdown: businesses believed their chances of getting caught, and its social, economic and political repercussions of this, had increased:
- ‘Now compliance has a “much bigger face”… ‘we see more companies disclosing offences, [there was] more coverup 10 years ago’ (March 2006).
- ‘Reputation drives behaviour for [the] big dealers’ (March 2006)
- ‘The reputational hit is higher [today]. [Their] perception of the chances of getting caught [are] higher. Cost of getting caught is [higher] too, in reputational and real terms” (March 2006).
- ‘There has been a change in cultures of compliance, … not caused by laws, but by …. investors (January 2006).
- ‘There’s been more ‘butt-covering’ [today] (January 2006).
- ‘The mere existence of law doesn’t affect compliance. But …there was no Compliance Subculture [5 years ago] (March 2006).

Regulators overall portrayed compliance as more problematic in smaller, newer firms than in larger, well established firms (Daniels and MacIntosh, 1991; Daniels & Morck, 1996). They expected, looked for and not surprisingly found more non-compliance there. Their own risk assessment documents reflect this: the first factor triggering a more extensive “Issue-oriented Review” is “…no active business, or little experience in its current business” (OSC Staff Notice 11-719, Page 5). Several reasons for focusing on smaller, newer firms were provided: “[large] companies usually have more checks and balances on individual behaviour than smaller market participants” (email communication, October 2006). And smaller firms, particularly venture companies, ‘do lower quality audits.’ Moreover, many such companies ‘were exempted from [government requirement establishing] independent audit committees’ (March 2006).

To accommodate these convictions, regulators distinguish the mainstream players, the 90% they identify as the law-abiding majority, from the 10% considered wilfully deviant. This majority is composed of actors and organizations who actually do comply, and those who want to but lack the knowledge or competence, usually new or inexperienced issuers. “Rogues”, on the other hand, are “one person bucket shops”,“’fly by night’ operators” or “international criminals operating through the internet” (Interviews January 2006). Regulator scrutiny is disproportionately directed here: this population is seen as most resistant to regulation and most likely to re-offend. (Interviews, January, February, May, 2006; email communication, October 2006)

Dominating the well-meaning 90% are those designated as “stakeholders”. These are the major corporate actors, large, established, mainstream companies - such as Enron, Worldcom, Nortel and Hollinger! “Stakeholders” are the experienced executives who sit on Advisory Boards and meet weekly or monthly with senior Commissioners and the

Executive Director. Their opinions are solicited when new policies are contemplated or problems arise. Their discourse permeates regulatory documents. Regulatory agencies act on the assumption that their stakeholders have the same vested interests in compliance as they do – an amazing belief given the immense financial payoffs of non-compliance.

From a traditional policing perspective, where deterrence through punishment is celebrated in rhetoric and policy, this rationale is problematic. The apriori credibility accorded (big) business assumes good faith. It legitimates a norm of consensual, education-based regulation, thus reserving criminal law for "the other", a tiny minority of miscreants. This is the regulatory perspective that produced Enron, it is the regulatory blind spot IMET and Bill C-13 were created to address! Such assumptions make it unlikely that mainstream blue-chip corporations will be meticulously scrutinized *or* pro-actively, regularly investigated outside equilibrium-upsetting crises and crackdown periods. Historically large mainstream corporations have been serial offenders, the most, not least likely to commit offences (Sutherland, 1983; Clinard and Yeager,1980; Coleman, 1987; Snider,2000; Rosoff et al, 2006). Indeed, more than 120 companies on the New York Stock Exchange are now under investigation for manipulating stock option grants, "spring-loading" and "backdating" their earnings statements (*New York Times,* November 5, 2006: B2). None of these are small, "fly-by-night" operations headed by inexperienced leaders.

2. Enforcement, Resistance and Criminalization

Enforcement, litigation and sanctions are thorny issues among regulatory staff, who recognize implicitly (not usually explicitly) the contradictions with their compliance mission. Those who spend their working lives cultivating good relations with business find their networks threatened when "stakeholders" are investigated or sanctioned. Such institutional tensions came through not in formal interviews, where everyone stressed agency unity, but in joking asides. For example, compliance staff introducing the head of enforcement said "now you'll get the views of the dark side" (March 2006). On another occasion a litigator referred to colleagues outside enforcement as "pussycats" (January 2006). Pre-and post-crackdown, enforcement staff pledge overall allegiance to compliance/education goals while simultaneously recognizing, accommodating and resisting the power of dominant stakeholder groups.

Enforcement staff had no problem describing their frustrations or the array of strategies companies employ against them. To counter such arsenals, security agencies use such techniques as SEDI, (the System for Electronic Disclosure for Insiders and Continuous Disclosure) to monitor trade patterns and flag suspicious activity, and the aforementioned computerized risk assessment protocols which target certain actors and business models for intensified scrutiny. Both the OSC and BCSC have Intelligence Units responsible for discovering problems in early stages of development.

Businesses, however, are skilled in the art of resistance. One frequent tactic is delay:
- 'They [business] try to induce "Regulator Malaise"' (February 2006).
- "It is in the interests of the Defence Bar to delay as long as possible" (February 2006).

- ‘Obstruction is aided and abetted by the Defence Bar’ (March 2006).

Delaying tactics work because memories fade and witnesses move away or die, but their primary impact is on cost. Delays cost money - and agencies have less money than most of their targets. With neo-liberal discourses equating speedy resolution with efficiency, regulators experience additional pressure to compromise and avoid prosecution whenever evidence is not crystal clear. And the chief job of defence lawyers is to make sure evidence is *never* “crystal clear”. This pressure for speedy resolution originates both internally (it is a Performance Measure) and externally, from the Defence Bar - ironically the body most responsible for delay.

Because the time and costs of prosecution are maximized when charges are pressed through external courts, agencies prefer to keep cases “in house”. Today, however, internal review panels face the same fierce resistance, “lawyering-up” and delay as external court cases:
- ‘The Commission [in internal proceedings] takes on quasi-criminal cases as well as regulatory matters. [But] they have become almost as protracted – everywhere roadblocks, [stables of corporate] lawyers… ’ (February 2006).

Reluctance to use the criminal justice system was widespread, solely because of its perceived lenience and inefficiency. Regulators voiced great belief in the *potential* of criminal law:
- ‘Criminal justice is a sham … it is way too slow’ (February 2006)
- ‘Sanctions are a joke. We have no sentencing guidelines or minimum sentences. For example this Newmarket guy was finally convicted, it was a $100 million fraud. He got 6 years and was out in 1” (February 2006).
- ‘There is no meaningful deterrence’ (February 2006).
- “We work hard on creating culture of compliance, [but] they develop *culture of non-compliance”* (March 2006).
- “Culture of compliance? How about a culture of *de*fiance!” (May 2006).
- ‘Wealthy people feel entitled. Money no longer means anything, power is what counts’ (March 2006).
- “we need a criminal response” (January 2006).
- “Punishment is what has [the most] effect. Concern over being jailed is key” (March 2006).
- ‘A lot of these guys are sociopaths…. it’s a kleptocracy! (March 2006).
- “I noticed a big difference [after the Bank of Nova Scotia raid]…. Guys who would not talk to me before were suddenly eager to make appointments” (March 2006).

3. “When the Pedal Hits the Medal”: The Defeats of IMET

IMET was the federal government’s most visible and tangible response to stock market meltdown. Regulators originally welcomed it, believing it would bring more resources, more criminal justice remedies and more regulatory “clout”. Unlike policing units in the past (Sliter 1994), IMET had “fenced funding”, monies exclusively reserved for securities fraud investigations, plus audits to prevent diversion of funds, and sophisticated

technological tools - PROOF, (Priority Rating of Operating Criteria) to assess and prioritize cases and MICA (Market Integrity Computer Analysis), with real time components to detect infractions. Although regulators felt IMET was "rushed" into existence for political reasons, they were "basically satisfied" with the overall design (Interviews, May 2006), and with the cooperation between their agencies and IMET:
- 'IMET are doing a good job…. [But] these are hard cases to investigate and prove.' (January 2006).
- '..a Good Thing to get RCMP involved again.' (March 2006).
- '.. too early to tell how [their] broader powers will be used. Might increase investor confidence, that's key' (March 2006).
- 'The enforcement process is more formalized since IMET …. [it] provides more market protection' (March 2006).
- 'We have good access to RCMP information. They find stuff and let us get involved earlier' (March 2006).
- 'They have a lot of clout if we need backup.' (January 2006).

However since its establishment IMET has shown itself to be a paper tiger, its potential effectiveness nullified by corporate power to stall and obstruct. Its explicit mandate, to tackle *major* cases of stock market fraud using criminal law, forces it into direct confrontation with major corporate players. IMET's targeted funding makes it difficult for the agency to divert resources or pick off easier targets – the 10% of offenders who are weaker and easier-to-convict. Restricting IMET to "big cases" pits it against transnational corporations with entire departments dedicated to devising ever more sophisticated legal challenges and impossibly novel strategies of defiance, obstruction and delay. The results were predictable: massive economic capital, plus corporate ability to *produce* "loss of confidence" by disinvestment, plus privileged access to Cabinet Ministers and media (corporate clout wielded as owners, major advertisers and/or professional networks) equals regulatory breakdown.

Thus IMET has faced "death by 42 boxes of documents" (May 2006). Swamping the agency in paper, sending emails and memoranda that have nothing to do with the investigation is standard corporate procedure, requiring days of costly person-hours to sort through. Mandatory disclosure rules, appeals challenging IMET's legal authority, suits to force IMET to pay the costs of providing documents to the defence, Charter challenges seeking corporate-friendly, precedent-setting decisions: all are regularly employed (May 2006).

IMET officers struggle to find non-structural explanations for their failures:
-*"The mandate [was]set extremely high"* 'It is now interpreted as [meaning that] every file has to affect the economy. This is a very high bar' (March 2006).
- 'We're being held to account because timelines were announced.' (March 2006).
- "We need to deliver – fast – on a few big cases" (May 2006)
- 'I think there should be … a National Securities Act – that would make [stock market fraud] a federal statute. This would give the RCMP a mandate to enforce" (May 2006).

Section IV: Accommodating Power:

The goal of this section is to link these empirical findings to theoretical claims. The dominance of compliance rationales shows how subterranean, non-formalized power relations form the regulatory terrain; crackdown periods show what happens when regulatory *habitus* is disrupted. .

1. Situating the Dominance of Compliance:

As we have seen, promoting market confidence through compliance is the primary regulatory rationale. Its centrality was stressed in agency documents and interviews by staff from every division. Even enforcement staff saw formal action as, at best, a necessary evil. This defensive mentality means that every regulatory initiative has to be justified to “stakeholders”. Framing the regulatory mission this way also empowers market players to demand a voice in policy-formation, and informs their implicit but unwavering assumption that they have a *right* to resist certain regulatory applications.

Regulators spend a lot of time and money trying to please, acting on their “common sense” belief in their obligation to: “avoid .. unnecessary demands on … market participants” (OSC Staff Notice 11-719, 2002: 3). They draw up performance criteria to measure their success and report back to stakeholders who would be considered “prospective offenders” in another frame. Policy documents are permeated with apologetic, defensive discourse, each regulation is excused, justified as necessary, functional and business-friendly. For example, OSC Staff Notice 11-719 (2002) informs “stakeholders” that the agency “much prefer[s] to foster compliance” (Page 3); its goal is to: “reduce regulatory burdens on [the] majority ….. who pose the lowest risk to capital markets” (Page 2). Advance notice of audits was necessary “to minimize [business] inconvenience” and demonstrate “good faith and respect for industry”. Thus prosecution was only justifiable for the most “extreme” or “flagrant” violations (interviews, January; March 2006). Using law to enforce regulations denoted regulatory failure, not success!

The contrast with Criminal Code prohibitions against theft, conspiracy and fraud is stark. It is impossible to imagine police justifying these laws, consulting weekly with ex-offenders, apologizing for enforcement or publicizing their enforcement strategies. Such postures only make sense if situated as *habitus,* as internalized responses to corporate power. Regulators have incorporated rationales constituting the corporate offender as a-typical and accidental, regulation as contingent rather than absolute, to accommodate the realities of their task, indeed to make their jobs *possible.* Bifurcating regulatory subjects into “stakeholders” and “rogues” legitimates their focus on the 10% whose lack of political and economic power makes them convict-able and sanction-able. These are the subjects who lack cultural, political and economic capital, those who are not invited to Monday morning briefings, who have no legal department to obfuscate and delay regulatory action. When read through the prism of corporate power, it becomes “common sense” to set “realistic” enforcement goals by targeting those with the least cultural capital. IMET provides an excellent example of the stultification that results when this tactic is not available.

Regulators without exception were well trained, highly educated professionals. They were keen to do the job - *as that job was defined*. The frame they simultaneously constitute and operate within constrains their agency, making it "realistic" to tread lightly around well-networked corporate actors and avoid targeting major corporations without "solid evidence". Unfortunately, this means such evidence can only be discovered *after* a corporate meltdown. Thus, while regulators exercise real power – they resist, challenge and accommodate "stakeholders" initiatives - this power is exercised within unacknowledged cultural, political, social and economic bounds. This invisibility makes these subterranean relations of power difficult to recognize or name, and therefore to shame, challenge or resist.

2. The Significance of Crackdowns: Effects on Enforcement and Resistance

Although the compliance-oriented rationales and assumptions established when securities agencies were first "thought" inform the routinized activities of the regulatory agency to this day, crackdown periods show what happens when regulatory *habitus* is disrupted. Such periods empower regulators – particularly enforcers and litigators - to act on the contradictions between the compliance mission of the agency overall and the enforcement missions of Enforcement/Litigation branches.

The "common sense" of bifurcation is most apparent when examining enforcement, for it is here that ideological barriers meet the tactical. Thus regulators, particularly enforcement staff, were well aware that the real impediments to going after major corporations were not legal. Too little law was never a problem. The main impacts of the crackdown at this level, four years after C-13 and SOX, were higher public expectations and heavier workloads:
- 'The new measures have had minimal effect.' (January 2006).
- "It will be hard to get convictions. It's all about Investor Confidence." (March 2006).
- 'There is no real crackdown' (February 2006).
- "Insider trading is "more show" than anything" (March 2006).
- 'We're busier"... not .. enforcing new laws …[but] taking on bigger cases' (March 2006).

What enforcement staff are recognizing here is that agencies always had the *official* power to enforce securities laws. In their words: 'All of these scandals could have been investigated *before,* with the sole exception of Insider Trading' (Interview, March 2006). What regulators lacked was the political, social, cultural and economic authority to pro-actively investigate dominant market actors. Outside crackdown periods, regulators are not free to define all rule-breakers as offenders, or to investigate all serious breaches of securities law. Pushback and resistance from dominant economic parties, at all levels, in diverse institutional, political and social arenas, is simply too strong.

Crackdown periods, by increasing the cultural authority of regulation, create a "window of opportunity", a transitory period when corporate push-back is less likely to be "heard" by mainstream media or government. At these times, regulators have permission to go after major players, to investigate pro-actively and prosecute. Enforcement is high

profile, making it harder for defendants to fashion plea bargains or negotiate "cut and run" deals. In Canada "our neighbour to the south" is lauded as a beacon of regulatory toughness contrasting unfavourably to Canadian "lenience". But outside crisis/crackdown periods US deregulating initiatives are lauded as an example to be emulated to avoid "capital flight"!

This paucity of cultural capital during "normal" times helps explain the blind spots of 1990s regulation - despite the best efforts of regulators. Enforcement divisions were concerned about what they saw as unsustainable profit levels and unrealistic hype, and made several unsuccessful efforts to increase their regulatory muscle (Interview, May 2006; *Globe & Mail,* October 20, 1999: B2; *Globe & Mail,* October 21, 1999: B1; *Globe & Mail,* October 27, 1999: B7.) Many insiders in financial circles and regulatory arenas suspected that "something funny" was going on at Nortel: post-crisis, its accounting "irregularities" became an IMET investigation (still unresolved). OSC personnel picked up rumours that accounting practices and expense accounts at Conrad Black's Hollinger Incorporated could not withstand scrutiny. Post-crisis this became a high profile criminal fraud trial initiated by the American Securities and Exchange Commission. But "everyone on [Bay] Street knew something was going on' (May 2006); 'there were all these rumours … [but] no one could *do* anything' (emphasis of interviewee, February, 2006). Similarly: "Before IMET, … the RCMP would not have taken this case [Nortel] .…. calling it a regulatory matter or leaving it to the US to prosecute" (email communication, October 2006). In other words, no high profile crisis, no permission to investigate pro-actively.

Conclusion:

Given the immensely successful resurgence of corporate power under neo-liberal regimes (Tombs & Whyte, 2002), its role in shaping the institutional priorities and "common sense" of regulators is not surprising. Corporate messages blanket public space, corporate sponsored research increasingly defines "knowledge", corporate free speech is legally protected (Glasbeek: 2002: 96). But this *habitus* is constantly being challenged and reconfigured. In this paper the disruptive potential of regulatory crackdowns has been investigated; however regional, local and national rivalries, shareholder rights groups and investigative journalists all challenge corporate hegemony (Barlow & Clark, 2002; Yaron, 2002). Electronically-based protest sites and blogs proliferate. These these factors, and many more, constitute new patterns of governance and (re)shape regulatory *habitus*.

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[1] Indeed, "as of March 2006, 48 Canadian companies were listed on the London Stock Exchange, of which the vast majority (36) were listed on the more "flexibly regulated" Alternative Investment Market ("AIM"). Of these 48 companies, 32 are also TSX-listed issuers, and 4 are TSX Venture Exchange-listed issuers" (Nicholls 2006: 135).

[2] Oil and gas, mining and financial services are still the economic bedrock, collectively making up more than 65% of total market capitalization on the country's largest exchange, the TSX (formerly the Toronto Stock Exchange) (Nicholls 2006).

[3] The BDA, in fact, was created to check OSC power – and to oversee trading in bonds, money market and over-the-counter equities. The Prospectors and Developers Association, which predated it, opposed the establishment of the OSC.

[4] The collapse of the major Wall Street investment bank Bear Stearns and the intervention of the US Treasury Department is the latest financial crisis. And it is producing the predictable debates over re-regulation (Andrews and Labaton, *New York Times,* March 23, 2008: 1, 9).

[5] The regulatory agencies discussed here assess fees for services from those they regulate. IMET is dependent on government funding, but their budget is partially protected through "fencing" , a system intended to keep it from being diverted to other uses.

[6] The law that came into force on September 15, 2004 stipulates: Section 380(1)(a) Maximum sentence for fraud over $5000 on indictment went from 10 to 14 years; (b) Fraud under $5000 if indictable, 2 year maximum; if summary, normal maxima apply – maximum $2000 fine or 6 month in prison. Section 380(2) makes fraudulently manipulating the public markets and indictable offence, maximum 14 years; insider tracing (382 1.1), indictable with a 10 year maximum; tipping (382 1.2) if by indictment, 5 year maximum; if by summary, normal maxima apply.

[7] Four "aggravating circumstances" are listed: a. fraud exceeds $1million; b. the "stability of the Canadian economy" or of investor confidence of any financial market was/could be affected; c. large number of victims; d. offender took advantage of community trust. The offender's reputation, skills or status are all deemed irrelevant if they were used to commit the offence.

[8] Its first arrest, in June 14, 2004, charged a man with "no fixed address"(!) with Theft over $5000 and Laundering the Proceeds of Crime. He is accused of selling 17 securities certificates from unclaimed accounts for $370,000 (RCMP News Release, June 14, 2004). A year later the Greater Toronto Area IMET team charged three senior corporate executives of the former Betacom Corporation with accounting fraud (www.rcmp.grc.gc.ca/on/press/2005/Jun14). The most recent charges, a "pump and dump" scheme were laid September 26, 2006. None of the high profile cases under investigation have produced charges.

[9] The new Chair of the OSC was CEO at the Bank of Nova Scotia when this raid occurred (Andrews, 2006: 67).

[10] Phrases with double quotation marks are direct quotes recorded *verbatim* during the interview or taken from emails sent by interviewees. Single quotations indicate material taken from the interview summary.