INNOVATION AND THE STATE

From social media to subprime mortgage-backed securities, innovation carries both risk and opportunity. It also throws up profound regulatory challenges. As it evolves, innovation continually undermines, circumvents, and sidelines regulatory structures designed to accommodate it. Here, Cristie Ford investigates the relationships between contemporary regulatory approaches and private-sector innovation, and considers the implications of both for broader social welfare priorities including equality and voice.

Regulation is at the leading edge of politics and policy in ways not yet fully grasped. Seemingly innocuous regulatory design choices have clear and profound practical ramifications for many of our most cherished social commitments. Innovation is a complex phenomenon that needs to be understood not only in technical terms but also in human ones. Ford argues for a fresh approach to regulation that recognizes innovation for the regulatory challenge it is, and that binds our social values and our regulatory tools ever more tightly together.

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Innovation and the State

FINANCE, REGULATION, AND JUSTICE

CRISTIE FORD

Peter A. Allard School of Law, University of British Columbia
Dedicated with immeasurable love and gratitude to my family
The bourgeoisie cannot exist without constantly revolutionizing the instruments of production, and thereby the relations of production, and with them the whole relations of society. . . . All fixed, fast-frozen relations, with their train of ancient and venerable prejudices and opinions are swept away, all new-formed ones become antiquated before they can ossify. All that is solid melts into air, all that is holy is profaned, and man is at last compelled to face with sober senses, his real conditions of life, and his relations with his kind.

Karl Marx and Friedrich Engels, *The Communist Manifesto*

The major impulses to successful financial innovations over the last twenty years have come, I am saddened to have to say, from regulations and taxes.

Merton Miller, ‘Financial Innovation: The Last Twenty Years and the Next’, *Journal of Financial and Quantitative Analysis*, 1986
In *Innovation and the State: Finance, Regulation, and Justice*, Cristie Ford provides a thorough analysis of the evolution of academic literature on ‘flexible regulation’ and couples this with an analysis of different forms of innovation to consider how regulation can fulfil progressive social goals whilst coping effectively with the risks and uncertainties that innovations within markets can pose. Elegantly written and perceptively observed, this is a timely analysis, which reminds us that regulation is a political and social project as well as a technical one.

Julia Black, Professor of Law, Pro Director for Research, and interim Director, London School of Economics and Political Science

A tour de force of innovation and financial regulation. Cristie Ford is street smart, experienced on Wall Street. She explains how sedimentary innovation is bound to defeat inflexible rulerish regulation. Yet sedimentary innovation also defeats flexible regulation, if it fails to fill the gaps that open within a scaffolding of regulatory principles. Ford’s brilliant book teaches us to learn to see financial innovation. It cautions political wisdom in building loyalty to public values as regulators steer economic interests.

John Braithwaite, School of Regulation and Global Governance (RegNet), Australian National University

Like the words ‘growth’ and ‘progress’, ‘innovation’ is often taken for granted as a public good. Indeed, it can be. But Cristie Ford shows in this deep and thoughtful book the way this taken-for-grantedness has seduced regulators, academics and the public into a set of beliefs that undermines the necessary task of regulation itself. She points the way forward to a more sophisticated interaction between regulation and innovation in a more just, progressive society.

Donald Langevoort, Thomas Aquinas Reynolds Professor of Law, Georgetown
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Abbreviations

ACBC      Asset-Backed Commercial Paper
CDO      collateralized debt obligation
CDS      credit default swap
CFPB      Consumer Financial Protection Bureau
CSE      Consolidated Supervised Entities
EMT      Efficient Market Theory
FASB      Financial Accounting Standards Board
FDA      Federal Drug Administration
FSA      Financial Services Authority (UK)
FSB      Financial Stability Board
FSOC      Financial Stability Oversight Council
GAAP      generally accepted accounting principles
HFT      high-frequency trading
IFRS      International Financial Reporting Standards
IOSCO      International Organization of Securities Commissions
ISDA      International Swaps and Derivatives Association
LTCM      Long-Term Capital Management
MMS      Minerals Management Service
NPM      New Public Management
NPR      National Program Review
OFR      Office of Financial Research
OMB      Office of Management and Budget
OTC      over-the-counter
PIG      public interest group
SEC      Securities and Exchange Commission
SPV      special-purpose vehicles
VaR      Value at Risk
WEF      World Economic Forum