The structural-informational power of business: credibility, signalling and the UK banking reform process

Scott James

To cite this article: Scott James (2017): The structural-informational power of business: credibility, signalling and the UK banking reform process, Journal of European Public Policy, DOI: 10.1080/13501763.2017.1349166

To link to this article: http://dx.doi.org/10.1080/13501763.2017.1349166

© 2017 The Author(s). Published by Informa UK Limited, trading as Taylor & Francis Group

Published online: 25 Jul 2017.

Article views: 79

Submit your article to this journal

View related articles

View Crossmark data
The structural-informational power of business: credibility, signalling and the UK banking reform process

Scott James

Department of Political Economy, King’s College London, London, UK

ABSTRACT
This article seeks to provide a better understanding of why business power varies over time and between firms. It assumes that business influence derives from firms’ ability to send credible information signals about policy costs, causing policy-makers to amend proposals. This ‘structural-informational’ power is mediated by two factors. First, the structure of the policy process enables policy-makers to assess the credibility of industry claims through institutional screening mechanisms, which vary over time. Second, the influence of individual firms is dependent on anticipated policy costs and past reputational damage, leading them to pursue different signalling strategies to maximize credibility. These claims are illustrated using the case study of United Kingdom banking reform between 2010 and 2013. Structural-informational power helps to explain why bank ‘ring-fencing’ reforms were agreed in the face of powerful industry opposition, but also why specific banks were subsequently able to extract important policy concessions.

KEYWORDS Banking reform; business power; information

Introduction
Theories of business power seek to explain why private firms occupy a privileged position in the policy process. From this perspective, business power is a constant structural variable that limits policy choices through the implicit threat of firm disinvestment. Yet this provides a limited explanation of how and why business influence varies over time and between firms. This article draws on structural-informational (SI) models of lobbying which suggest that business power derives from a firm’s capacity to transmit credible information signals to policy-makers about the costs of policy change. It develops a framework for analysing the factors that mediate the structural-informational power of business. First, the article argues that the policy process is an...
important determinant of business power over time, enabling policy-makers to assess the credibility of industry claims through institutional screening mechanisms. Second, the influence of individual firms is dependent on anticipated policy costs and past reputational damage, leading them to pursue different signalling strategies to maximize their credibility. This provides a more fine-grained analysis of how business is able to extract specific policy concessions from policy-makers.

The framework is illustrated using the case study of United Kingdom (UK) banking reform between 2010 and 2013. In June 2010, the newly elected Conservative–Liberal Democrat coalition government announced the creation of an Independent Commission on Banking (ICB), chaired by the former Bank of England Chief Economist, Sir John Vickers. The ICB was tasked with making recommendations on structural reforms that would promote both stability and competition in banking. Its final report, endorsed by the government, heralds a major shake-up of the industry (ICB 2011b). The reforms require UK banks’ retail activities to be placed in an operationally separate ‘ring-fenced’ subsidiary which is no longer permitted to trade most derivatives and securities, and which must comply with stringent new capital requirements. Yet the final legislation, enshrined in the 2013 Financial Services (Banking Reform) Bill, differs in several important respects from the ICB’s original proposals. The article uses SI power to explain why structural reform was agreed in the face of opposition from the most powerful banks; but also why specific banks were subsequently able to extract important policy concessions to minimize the impact of ring-fencing.

The article begins by briefly reviewing the business power literature, and then outlining the theoretical framework and case study method. The analysis that follows is organized into two sections. The first shows how industry influence was constrained by screening mechanisms during the ICB process, paving the way for early agreement on structural reform. The second section details how the subsequent Treasury process was much less effective at screening industry claims, enabling the banks to pursue signalling strategies aimed at extracting concessions to minimize the impact of ring-fencing. The article concludes by reflecting on the added value of the SI framework.

Theories of business power

Theories of business power suggest that business influence derives from two main sources. The first, instrumental power, is concerned with observable qualities of power relations, such as lobbying and campaign contributions. The second, structural power, recognizes that governments are dependent on their investment decisions to sustain economic growth and fund public services (Lindblom 1977; Przeworski and Wallerstein 1988; Swank 1992). In anticipation of negative inducement effects, and the wider electoral and
fiscal consequences, policy-makers avoid policies that threaten to undermine business confidence. As a result, business interests enjoy an over-proportionate consideration in the formulation of policy, even if firms abstain from direct political activity.

Empirically, however, these claims have proven problematic. Hacker and Pierson (2002: 281) criticize the assumption that business pressure is a constant background variable that is generated systematically by an ‘investment veto weapon’. It is self-evident that business has to actively lobby to exert influence and that it does not always win in battles with government (Smith 2000). Important studies have therefore sought to qualify business power. From an institutionalist perspective, Streeck and Schmitter (1985) argue that the configuration of state authority, bureaucratic interests, legal norms, informational needs and sectoral specificities shape the organizational properties of business lobbying. According to this ‘logic of influence’, the state is capable of selecting and moulding interaction with business to serve its longer-term functional imperatives. By contrast, constructivists view business power as inter-subjectively constructed by government actors that use ideational lenses to confront, interpret and react to business pressures (see Bell 2012; Hay and Rosamond 2002). Applying this framework to the banking sector, Bell and Hindmoor (2015) show how bank power has been constrained by the enhanced capacity of the state, the increasingly politicized regulatory environment, and declining threat perceptions amongst policy-makers.

Culpepper and Reinke (2014) distinguish sources of business power (structural vs instrumental) from how they are mobilized (automatically or strategically). From this perspective, structural power often has to be asserted strategically. For example, firms may use their lobbying resources to deliberately amplify policy-makers’ concern over disinvestment by making claims about the detrimental economic impact of new regulations (Fairfield 2015: 422). Equally, a firm’s structural position in the economy directly shapes its bargaining strength in negotiations with policy-makers (Culpepper and Reinke 2014: 436). Applying this framework to bank bail-outs in the UK and the United States (US), they argue that those institutions capable of asserting their structural power strategically secured the best deal from government. Alternatively, Woll (2014) suggests that bank influence is rooted in their power of ‘inaction’, forcing policy-makers to engage with institutions on a one-to-one basis and producing suboptimal regulatory outcomes.

Despite these important innovations, there are two aspects of business power which remain under-specified. First, to demonstrate a causal effect, empirical studies must show how variation in structural power over time produces meaningful changes in policy-maker behaviour and/or policy outcomes (Culpepper 2015: 396). In particular, greater attention is needed to show how institutional features of the policy process mediate business power by structuring the rules of interaction with firms. Second, structural power provides
a limited explanation of the variability of firm influence. In reality, the threat of disinvestment is an option available to very few firms because the costs of ‘exit’ are prohibitively high. Moreover, such threats are neither fixed nor exogenously determined; rather, they are discursively constructed by business (Farrell and Newman 2015). A more fine-grained analysis of business agency is needed to explain how firms make credible structural claims to policy-makers (Young 2015).

To address this, the article draws on structural-informational models of lobbying. This is used to develop a framework for testing general claims about the variability of business power that could be applied to a wide range of policy cases.

**Structural-informational power**

Informational models start from the assumption that lobbying is about the strategic transmission of information (Austen-Smith 1993; Bernhagen and Bräuninger 2005; Bernhagen 2007; Grossman and Helpman 2001). Policy-makers need access to detailed information and expertise to develop and implement policy, yet it is scarce and costly to generate. By contrast, business has privileged access to policy-relevant information which derives from everyday market activities and pooled research. This structural-informational advantage enables business to supply privately-held information to policy-makers and provides an opportunity to shape the policy process.

The real source of structural power derives from the incentives that information asymmetries create. Business tends to be risk averse about new policy developments and therefore has an incentive to misrepresent the size and likelihood of a policy’s negative effects (Bernhagen and Bräuninger 2005: 46). Policy-makers know that policies impact differentially on firms, imposing high costs on some but low or zero costs on others. The challenge they face is to assess the veracity of these claims and to decipher honest from exaggerated messages. In this partial conflict of interests, a signalling game ensues: business must assert that a particular policy will generate an adverse reaction by firms; but to exert a causal effect on policy outcomes, these claims must be assessed as credible by policy-makers, leading them to modify or drop the policy proposal (Bernhagen and Bräuninger 2005: 48). Business influence derives from its structural-informational power, defined as the capacity to transmit credible claims about the economic cost of public policy.

SI power permits a more fine-grained analysis of variability in business influence. The first source of variation stems from the capacity of policy-makers to assess the credibility of business claims. Given the highly technical and firm-specific nature of the information that firms supply, policy-makers are rarely able to verify industry arguments directly (Bernhagen 2007). They must therefore rely on a proxy or ‘signal’ of credibility. Signalling theory
tells us that this comes from the level of costly political action that a firm is willing to incur in an attempt to influence policy-makers; for example, by commissioning detailed research and analysis to support their position, or by galvanizing wider opposition through public relations activities (Grossman and Helpman 2001: 143–4). A firm’s willingness to undertake costly political action therefore conveys a useful information signal to policy-makers about the veracity of their claims.

Importantly, policy-makers can manipulate the level of costly political action that firms must undertake when lobbying. In signalling theory, a player can reduce information asymmetries with another player through screening. Screening is a mechanism for extracting useful private information from another player by observing the choices they make. Widely used in contract theory and labour economics, screening can encourage other players to signal honestly, and/or block or filter out dishonest signals, by reshaping incentives (Spence 1973). For example, employees can use screening mechanisms – such as interviews or tests – to discriminate between job applicants to find those with hidden desirable qualities, such as a high work ethic. Surprisingly few studies have considered the importance of screening mechanisms in the policy process. For example, policy-makers can impose direct costs on firms by demanding campaign contributions in return for access (Grossman and Helpman 2001: 171–84). More subtly, the structure of the policy process can mediate, filter or ‘jam’ industry signals by configuring the rules of the lobbying game. Policy-makers are embedded within wider institutional structures that provide valuable political or financial resources, which can be used to accumulate technical knowledge and expertise. The policy process also structures the form and channels through which private information is supplied, how it is processed and interpreted, and the extent to which it is scrutinized. For example, delegation of regulatory decisions to autonomous agencies can help shield policy-makers from short-term pressures generated by both business and elected officials. In addition, visibility and communication by policy-makers can raise awareness of salient issues, expose industry lobbying tactics, and facilitate mobilization of non-business groups. In signalling terms, the policy process is therefore an important determinant of policymakers’ capacity to assess, challenge or even rebut industry claims.

Screening mechanisms do not necessarily allow policy-makers to directly verify industry claims, as these are based on privately held information. But they can raise the level of costly political action firms must undertake by forcing them to transmit more and better-quality information to support their claims. In effect, screening mechanisms raise the price of admission for firms seeking to influence the policy process (Grossman and Helpman 2001: 144). This has important implications for business power. When firms do not need to undertake costly political action in order to lobby – because screening mechanisms are weak – most firms will have an incentive to
oppose the proposal, regardless of whether the actual policy costs to the firm are high or low. Moreover, firms facing low policy costs will have a tendency to exaggerate the costs of policy change (Bernhagen 2007: 66–9). In this situation, policy-makers know that some firms have a tendency to exaggerate, but they have little basis for differentiating honest from dishonest signals. Business therefore has the upper hand because policy-makers can glean little useful information about credibility from the willingness of firms to lobby (Grossman and Helpman 2001: 161). However, as firms must undertake higher levels of costly political action to lobby – because screening mechanisms are strengthened – this produces differential payoffs for business. Firms facing high policy costs will continue to have a strong incentive to lobby against the policy proposal, but firms facing low policy costs may now have little or no incentive to do so because the resource implications of lobbying become prohibitively high (Bernhagen 2007: 66–9). In this situation, the power of business is reduced as policy-makers can interpret the credibility of industry claims from the willingness of firms to pay the higher admission price into the policy process. Policy-makers therefore have the upper hand because they are more likely to receive honest signals from firms. We test the claim that the nature of the policy process shapes the degree of business influence over time.

The second source of variation in SI power is the ability of individual firms to signal credibility to policy-makers. Drawing on formal signalling models, the framework presented here suggests that this is a function of the anticipated policy costs they face in the future, and the reputational damage they have incurred in the past. Policy costs refer to the expected directly incurred costs of a new policy proposal on a firm (Bernhagen 2007: 69). For example, this may include internal restructuring, regulatory compliance or prohibition of certain activities, all of which are likely to impact on profits and shareholder value. High anticipated policy costs serve as a powerful incentive to firms to undertake costly political action in an effort to signal to policy-makers that their concerns are genuine. Reputational damage reflects the fact that lobbying is a repeat game. Firms therefore have an interest in upholding a reputation as a reliable and trustworthy source (Kennan and Wilson 1993: 46). If firms have been exposed as making exaggerated or dishonest claims in the past, this inflicts reputational damage which diminishes the ability of a firm to signal credibility in the future. The framework suggests that firms will pursue different signalling strategies, based on the balance of anticipated policy costs and past reputational damage that they face, in order to maximize their credibility in the eyes of policy-makers.

The article proposes a simple typology of signalling strategies (see Figure 1). Assuming that policy costs and reputational damage can be either high or low for any firm, this produces four quadrants. These provide a basis for explaining how individual firms assert SI power, based on the
observable signalling strategies that they pursue. Intuitively, a firm with high policy costs and low reputational damage is in the strongest position to signal credibility: they have a powerful incentive to devote resources to undertaking costly political action, and are considered trustworthy by policy-makers. We would therefore expect these firms to be the most assertive in lobbying policy-makers, pursuing signalling strategies of ‘defiance’ in opposition to policy change. By contrast, firms with low policy costs and high reputational damage have little reason to oppose the policy; nor are they capable of signalling credibility because they are distrusted by policy-makers. In this weakened position, the framework predicts that a firm will choose to support the proposal and will play a constructive role in its development (this is labelled ‘accommodationist’ signalling). Such a decision is a strategic move aimed at building trust with policy-makers and restoring an organization’s damaged reputation. Firms in the other two quadrants face mixed incentives. For example, those with low policy costs and low reputational damage have the potential to wield influence as they are respected by policy-makers, but they have little direct incentive to do so. As a consequence, they will therefore remain largely on the sidelines (‘minimalist’ signalling). Conversely, a firm with high policy costs and high reputational damage has a powerful incentive to oppose the policy, but is constrained from doing so owing to its tarnished reputation. In this situation, a firm will try to leverage its limited influence by seeking alliances with others in an effort to free ride on their credibility (‘collaborative’ signalling). Although collaboration involves the investment of considerable time and resources, this will be outweighed by the potential benefits of greater policy influence.

Figure 1. Bank signalling strategies during UK banking reform.
The SI approach does not view policy costs and reputational damage as fixed, but as dynamic and subject to change over time in response to both exogenous and endogenous factors. For example, policy-makers can withdraw or amend policy proposals in response to industry or political pressure, which alter the anticipated policy costs to individual firms. Reputational damage can also change suddenly as regulatory failures are revealed, providing focusing events for public outrage. Shifting policy costs and reputational damage over time reconfigures the SI power that firms are capable of asserting; in response, firms would be expected to revise their signalling strategies.

The framework is applied by analysing the UK banking reform process. The concept of SI power enables us to make a clearer empirical distinction between the exogenous structural ‘position’ of business in the economy, which in the case of the banking industry remains formidable, and the endogenous structural ‘claims’ made by lobbyists, which have changed significantly since the financial crisis. The typology of business signalling strategies leads us to predict that banks with high policy costs/low reputational damage will be able to extract the most concessions on banking reform from policymakers; by contrast, banks with low policy costs/high reputational damage will be able to extract the least. The research for the article is based on 62 anonymized interviews conducted between 2012 and 2014 with senior officials from Her Majesty’s Treasury and the Bank of England, former members of the ICB, lobbyists from the five main UK banks, and financial industry trade associations. The analysis that follows begins by examining bank influence following the establishment of the ICB in 2010, and then analyses the subsequent Treasury-led consultation process from 2011.

**Bank signalling during the ICB process**

UK banking reform provides important support for the basic assumptions of the SI model. It is evident that policy-makers are highly dependent on private information about the impact of policy change. A senior regulator confirmed that ‘fundamentally the banks are the source of all the information we need to get’, so the main challenge is deciphering whether industry concerns are genuine or not.¹ Effective lobbying is viewed by policy-makers as ‘intellectually honest and unexaggerated’ because it provides an early warning when they are ‘getting things wrong’.² To assess credibility, officials look to signals about the quality of the information supplied:

> You’re very sensitive to is the information new? Is the information well argued? … We’d be most influenced by things that we thought were robust, that were telling us information that we didn’t already have, that were analytically rigorous.³

For lobbyists, the most effective way to signal credibility is to produce detailed research and analysis, much of which is commissioned by external economic
consultancies. But credibility is also viewed as a function of reputation accumulated over time, which is damaged by repeated exaggeration:

They say don’t do this it will be dreadful. Then you do it and they move on. They don’t quite realise that this creates the impression that they’re bullshitting and exaggerating … which is a really bad strategy because it’s a repeat game.4

The ICB relied on two main sources of private information supplied by the banks. The first sought the views of the banks on the ICB’s terms of reference, measures to enhance financial stability, and the prospect of structural reform. This was gathered through an initial call for evidence which required banks to respond to a detailed survey questionnaire and supply long-run financial data. The second category was financial information related to bank business models, used to assess the impact of different reform options. This required regular working-level meetings with bank officials and frequent information requests issued by the ICB. To facilitate this, the largest banks established secure online ‘data rooms’ so that information could be viewed on a confidential basis. In addition, away-days to bank head offices were organized for ICB officials:

We brought the entire secretariat to the bank for whole days to walk them through the operation of the bank … We wanted them to proceed from a truly informed perspective, and were willing to spend a lot of time teaching them how to do it.5

Despite the information advantage wielded by the banks, the ICB served as a highly effective screening mechanism of industry signals. Three factors were critical in enabling it to do so. First, delegation of the process to an independent committee helped to insulate policy-makers from both industry pressure and elected officials. With a finite existence and no policy-making powers, the ICB’s engagement with the banks became a single-shot game; it was therefore viewed by lobbyists as very independently minded and ‘immune’ to industry pressure, creating the impression that the ‘conclusion had already been hard wired into the process.’6 The status of the commissioners, two of whom were former bank executives, also provided an ‘insurance policy’ against the banks deliberately attempting to mislead.7

Second, although the ICB was lightly resourced with a 14-strong secretariat, it was able to accumulate considerable expertise by issuing two separate calls for evidence over an extended period. The quantity and quality of information it sought to gather was much closer to that of a Competition Commission investigation, forcing banks to devote vast resources to the process. Compared to a standard regulatory consultation, which typically lasts three months, the ICB process was of a different order of magnitude: ‘We’re talking literally thousands of man-hours in terms of the number of people involved, and the scale and size of the information we gave them.’8 The
informational demands placed on the banks were viewed as a mechanism for filtering out unsubstantiated arguments: ‘I think the Vickers process filtered a lot of that out because the consultation documents were very long and they posed some pretty difficult questions.’9 In addition, the ICB commissioned its own quantitative analysis on the impact of ring-fencing from independent City analysts, enabling it to directly verify bank claims against their own cost–benefit estimates.

Third, an important innovation was that senior bank executives attended closed hearings with the ICB, deliberately conducted in the style of a full competition inquiry. This reliance on formal written submissions and structured hearings constrained the ability of industry to wield influence through pre-existing informal channels:

What the ICB process did was reshape the received wisdom about the process. We had to work out afresh what the process will look like, when to engage, and how that needed to happen. It was the novelty of the process which had the most impact by challenging the way we normally sought to influence decision makers.10

The article argues that the ICB served to reduce the SI power of business by strengthening the screening of industry claims. As the process demanded more and better quality information from the banks to support their arguments, industry was forced to undertake a higher level of costly political action in order to lobby policy-makers. On occasion, the ICB was even able to expose industry’s tendency to exaggerate by directly rebutting its claims about policy costs. For example, in 2011 the banks jointly commissioned a report from Oliver Wyman which estimated the cost of structural reform to be between £12 bn and £15 bn.11 Yet the credibility of these claims was directly challenged by the ICB, which calculated the cost to be a more modest £4–5 bn (ICB 2011a). On another occasion, ICB officials ‘took apart’ the figures submitted by one bank, which had the effect of halving the economic costs they had claimed.12 The banks acknowledged that they struggled to produce credible figures for the economic costs of reform, concerned that attempts at ‘bogus precision’ risked being exposed.

The SI framework predicts that effective screening creates differential payoffs for firms: those facing high policy costs have an incentive to continue lobbying, but those facing low policy costs will be less willing to bear the costs of doing so. As one lobbyist confirmed, by late 2010 those banks that were only marginally affected by ring-fencing decided not to oppose reform because ‘it would just cost too much to produce the evidence.’13 Consequently, attempts to maintain a united front broke down as the banks increasingly sought to represent themselves to try to secure special treatment:
We definitely did not discuss the detail of our positioning with anybody because there were very different views … I was surprised at the speed with which some of the other banks were falling over themselves to agree with ring-fencing. They were adopting a political position.\footnote{14}

This strengthened the position of policy-makers because they could glean useful information from the (un)willingness of firms to undertake costly political action. As one ICB official noted, ‘When we didn’t get evidence, that was useful … A bank not giving you a robust answer to something means that maybe there isn’t a defensible reason for not doing something. So you can give more confidence to actually do it.’\footnote{15} For example, the failure of the banks to provide the ICB with hard evidence supporting their claims about the economic benefits of universal banking was cited as a key reason why the commission opted for ring-fencing. Moreover, as the banks increasingly sent mixed signals, so policy-makers were better placed to differentiate honest from dishonest signals: ‘[The banks] would say things that would contradict each other. And that was often quite useful because you can go that’s rubbish, because I’ve just heard someone else say the completely opposite thing.’\footnote{16}

By constraining the SI power of business, the ICB was able to build political momentum for structural reform and secure early agreement from the government that ring-fencing would be implemented. In the following section, we explore how the dynamics of the signalling game subsequently altered, enabling the banks to extract significant concessions from policy-makers.

Bank signalling after the ICB process

Following the publication of the ICB Final Report in September 2011, the banking reform process was handed back to the Treasury. In drafting the final legislation to implement ring-fencing, officials conducted a series of consultations with industry stakeholders. Having lost the broader political argument about structural reform, the banks recognized that their ability to influence policy lay in shaping the final design of the ring-fence. The bulk of their lobbying effort – around 80–90 per cent according to one lobbyist – was therefore devoted to targeting Treasury officials during the post-ICB process.\footnote{17}

The Treasury process differed in three fundamental respects from the ICB. First, engagement with industry was less structured and more informal, allowing the banks to exploit ‘regular contacts and existing relationships’ to push back against the reforms.\footnote{18} Second, the process was less insulated from elected officials. Because the banks enjoyed ‘higher influence in government than they did with the independent body’, the ICB recommendations could be ‘watered down’.\footnote{19} Third, officials’ lack of resources and expertise meant that the Treasury was highly dependent on private information and had little basis for assessing its credibility:
There’s a huge information gap. The people at the Treasury are not banking experts … Certainly what I’ve seen is that the Treasury goes to the banks and says ‘well how does this work, can you teach us how this works?’

This provided an opportunity for banks to ‘educate’ policy-makers by providing informal teaching sessions:

The Treasury team were seriously inadequate … We made a very early offer to bring people in and do teach-ins, and they absolutely jumped at it. We had the whole entire team over here on several occasions to work through the implications of other policy options.

We argue that the Treasury process was less effective as a screening mechanism of private information because it was characterized by informal structures of engagement, less autonomy from elected officials, and limited knowledge-based resources. This had the effect of lowering the level of costly political action firms had to undertake in order to engage in the policy process. As a result, policy-makers had little basis for assessing the credibility of industry claims as they could glean little useful information from the willingness of firms to lobby against the reforms. The SI power of business was therefore significantly strengthened.

To explain the policy concessions subsequently extracted by the industry, the article analyses the signalling strategies pursued by individual banks during the Treasury process. It provides confirmation that these are determined by a firm’s assessment of policy costs and reputational damage. Banks decide what level of lobbying resources to allocate to an issue based on two ‘filters’: the first relates to ‘interest and enthusiasm level’ or the ‘material impact’ of the proposed policy; while the second concerns the banks’ reputation or ‘political capital in government’. Each bank faced a different mix of costs, generating incentives to send different signals to policy-makers about banking reform. Using the simple matrix of high/low costs outlined above, we can categorize the signalling strategies based on four main types (see Figure 1).

Banking reform threatened to impose high policy costs on three universal banks: HSBC; Barclays; and RBS. For Barclays and RBS, the reforms threatened to significantly increase the costs of separately funding their investment banking operations, while for HSBC the prospect of complying with new loss absorbency rules at group level was highly problematic because of its large overseas assets. Although they all had a strong incentive to lobby hard against change, the three banks sent different signals to policy-makers as they faced variable levels of reputational damage. HSBC and Barclays, having avoided direct taxpayer-funded support, could initially afford to ‘lead the charge and be more vocal’ in their signalling strategies. In particular, HSBC was able to signal greater credibility than any other bank for two reasons. First, the bank launched a periodic internal review on moving its
head office to Hong Kong, an exercise designed to signal that its threat to dis-invest was a credible one. Second, the bank invested heavily in undertaking high-quality research to make rigorous and ‘highly influential’ submissions.23 Hence, as one lobbyist explained, ‘HSBC were head and shoulders above everyone else given that they had the most solid business model, so they’re taken seriously and listened to.’24

Its experience illustrates how the SI power of banks varied over time. During the ICB, HSBC made little headway convincing officials that its business model necessitated special treatment regarding new Primary Loss Absor-bency Capital (PLAC) requirements: ‘We told them, we’re not like any other bank. But they just didn’t listen … This was really, really bad. This was a “are we going to have to quit Britain moment because this is two billion dollars a year” moment.’25 Yet HSBC later received a more favourable response from the Treasury, enabling it to secure an exemption for all overseas assets:

The Treasury process was good because it weeded out some of the extremes … We had a very good conversation with them. They asked us for our issues and then sat down and discussed those. Group PLAC was the big issue for us and they recognised that it didn’t work … So they gave up on that idea and quietly brushed it under the carpet.26

By contrast, the SI power of Barclays diminished over time. At the start of the process, the bank’s CEO, Bob Diamond, was an outspoken critic of structural reform and claimed that the bank might be forced to relocate its investment operations to New York. Yet this early signalling strategy of ‘defiance’ was undermined when the bank was directly implicated in the manipulation of the London Interbank Offered Rate (Libor) in 2012. The reputational damage that this inflicted undermined Barclays’ credibility. Policy-makers came to the view that the bank had ‘escaped paying the price’ for engaging in high-risk trading behind an implicit government bail-out, and so they ‘started to get tired of their threats to pull out’.27 In a sign of Barclays’ waning influence, its attempt to corral industry into supporting operational subsidiarization as an alternative to ring-fencing ended in failure. To policy-makers, the proposal lacked credibility as there was insufficient ‘common ground’ across industry, and because it ‘delivered none of the benefits of ring-fencing and avoided all the costs’.28 In response to increasing reputational damage stemming from the Libor scandal, the bank was forced to abandon its ‘defiant’ signalling strategy and pursue a more ‘collaborative’ approach instead.

A second bank that pursued a ‘collaborative’ signalling strategy was RBS. As a symbol of the bank bail-outs, RBS’s voice was greatly diminished and it struggled to advance a ‘credible position’.29 Although it commissioned independent research about the costs of ring-fencing to boost its credibility, the bank’s reputation prevented it from being used publicly ‘because our
executives didn’t feel terribly comfortable with it. For both RBS and Barclays (after the Libor scandal), collaboration meant trying to leverage their influence through more powerful others:

We contacted Standard Chartered because they had some quite strong views and were influential. We thought that they were better positioned to make those points than we were... We were thrilled that they pitched in because we weren’t in a position to make strong arguments.

Collaboration also involved the main trade associations. The value of the British Bankers’ Association (BBA) had been fatally undermined by the Libor scandal, however, which left it ‘severely reputationally damaged’ and with ‘zero credibility’ in the eyes of policy-makers. Instead, the banks leveraged their credibility through the wider business community. For example, Barclays worked closely with the Confederation of British Industry (CBI) because they were a more ‘credible voice’ given their ability to represent the interests of industry as a whole. The CBI’s claim that structural reform would damage the manufacturing sector by restricting lending resonated in government, enabling them to secure a commitment to delay implementation to 2019.

They were also effective in campaigning for a broader range of financial products to be provided by ring-fenced banks. Business representatives worked closely with Treasury officials to help them define simple derivative products, enabling them to secure important changes to the legislation. As a bank lobbyist acknowledged, this was a victory ‘they won, rather than us’.

The other UK banks had low policy costs from structural reform because of the limited impact of ring-fencing. The signalling strategies they adopted can be further sub-divided, based on the reputational damage they had incurred from the financial crisis. The first group, including Santander and Standard Chartered, did not receive direct government support and so their reputations remained largely intact. For example, Santander had little incentive to proactively lobby policy-makers because of its retail-based business model. As it preferred to ‘keep its head below the parapet’, the bank was therefore slow to engage in the process and did not devote extensive resources to lobbying on banking reform (a ‘minimalist’ strategy). By contrast, the signalling strategy pursued by Standard Chartered changed suddenly during the process. At the start, the bank’s chief executive officer (CEO), Peter Sands, signalled ‘defiance’ by being highly critical of structural reform and threatening to shift operations to Singapore. This decision to take a hard line ‘succeeded in delivering a positive outcome’, as the bank secured a de minimis threshold for UK bank assets which excluded all of its operations from the ring-fence. Having drastically reduced the anticipated policy costs of banking reform, Standard Chartered had less incentive to continue lobbying. It therefore reverted to a ‘minimalist’ strategy and remained largely on the sidelines for the rest of the process.
Lloyds was similarly relaxed about the prospect of retail ring-fencing, but the bank’s credibility had been severely dented by its receipt of taxpayer support. As predicted by the model, it took an early strategic decision to break ranks with the rest of industry and support ring-fencing in an effort to restore its reputation with policy-makers. Lloyds was ‘assiduous’ in its engagement with policy-makers because ‘we wanted to appear as a credible and trusted witness so that we could achieve what we wanted to achieve’.37 This strengthened the hand of policy-makers because Lloyds was ‘more pliable’ and it was ‘easier to get information out of them’.38 Intriguingly, however, this ‘accommodationist’ strategy was also a deliberate attempt to shape the reform agenda: ‘Lloyds was the only bank in the pro-reform camp because, cynically, we preferred the debate to be dominated by the ring-fencing agenda rather than the competition agenda.39 To pre-empt calls for a competition inquiry, Lloyds successfully persuaded officials to adopt its proposal for a seven-day current account switching service:

We wanted to offer something that they could support … They were looking for a solution, and to have one provided by the biggest players suited them. The fact that they could then sell that to politicians was a big win for us.40

This shrewd signalling tactic paid off, as Treasury policy-makers decided to ignore the ICB’s recommendation that Lloyds undertake further branch sell-offs.41 By providing political support to policy-makers for ring-fencing, the bank was therefore able to secure a significant concession on a separate but related policy issue around which it had much greater concerns.

As predicted by the framework, the banks pursued different signalling strategies based on the balance of anticipated policy costs and past reputational damage. Given the strengthened SI power of industry during the post-ICB process, this enabled them to extract important policy concessions aimed at reducing the impact of ring-fencing. Banks with high policy costs and low reputational damage were defiant in their lobbying (notably HSBC and Standard Chartered) and were the most successful at securing firm-specific changes to the legislation. By contrast, the reputational damage sustained by Barclays and RBS constrained their influence, forcing them to pursue a more collaborative approach through the CBI to secure moderate changes to the ring-fencing rules. As expected, Lloyds took the strategic decision to support structural reform and provide ready-made policy solutions. Surprisingly, however, this accommodationist strategy proved more effective than predicted by the framework; not only enabling the bank to restore its reputation in the eyes of policy-makers, but also allowing it to gain a significant ‘win’ in a linked policy issue.
Conclusion

UK banking reform provides a useful illustration of the limits of traditional theories of structural power. Explanations that rely on threats of disinvestment fail to explain why the financial industry was unable to resist reforms which imposed significant new costs on industry. More puzzling still is the fact that the ICB’s recommendations impact the most on those banks that were not bailed out (HSBC and Barclays) and which might have been expected to have used their power of ‘exit’ to block reform. Problematically, structural power explanations therefore provide little clue as to why some banks in a strong structural position had limited influence (Barclays) or chose not to engage in the process (Santander), while some bailed-out banks managed to extract significant concessions (Lloyds). This article’s central claim is that variation in business power can be better explained through the concept of structural-informational power.

The SI framework developed here makes two important contributions. First, it specifies how mediation by the policy process can cause business power to vary over time. The results show that powerful screening mechanisms can empower policy-makers by forcing firms to undertake increasingly costly political action, in the form of transmitting more and better quality information. This strengthens the capacity of policy-makers to scrutinize the credibility of industry claims by creating incentives for firms to send only honest signals. The analysis highlights the importance of three institutional factors: autonomy from elected officials; knowledge-based resources; and formal structures of engagement. This has important implications for theories of regulatory capture. In particular, it suggests that the structural-informational advantages that business derives from pooling their resources can be challenged through the design of robust policy processes which raise the costs of lobbying, thereby creating incentives for firms to compete against one another for influence. Future research would do well to examine the relevance of the three institutional variables across ‘most different’ policy fields in order to test the generalizability of the framework.

Second, the article offers a more fine-grained analysis of how business power varies between firms. The framework proposes that the SI power of firms is a function of the balance of anticipated policy costs and past reputational damage. The typology that we develop sheds new light on how individual firms pursue different signalling strategies in an effort to signal credibility and extract specific policy concessions. The first, associated with signalling strategies of defiance, relates the most closely to traditional forms of structural power as it relies on firms sending credible signals about high policy costs and threats to disinvest. This strategy enabled banks like HSBC and Standard Chartered to negotiate important exemptions from the new ring-fencing rules. Second, firms may leverage their power through front organizations which
are viewed as more credible by policy-makers. Our illustration of how weakened banks (Barclays and RBS) used the CBI to amend and delay banking reform shows how effective this can be. Third, SI power may be asserted when firms supply credible information to policy-makers in return for policy concessions in a related area. In the case of Lloyds, providing political support to policy-makers on ring-fencing can be viewed as a form of side payment, designed to exploit issue linkage by securing a more favourable policy outcome in other areas, such as competition. Crucially, in all three cases – threats to disinvest, front organizations and side payments – the structural power of business was dependent on the supply of credible information to policy-makers. Further investigation of these subtle but significant forms of SI power is essential to develop a more sophisticated understanding of how business shapes public policy.

Notes

1. Interview, 8 August 2013.
2. Interview, 12 April 2013.
3. Interview, 8 August 2013.
4. Interview, 12 April 2013.
5. Interview, 25 September 2013.
6. Interview, 10 May 2013.
7. Interview, 10 April 2017.
8. Interview, 18 September 2013.
9. Interview, 14 October 2013.
10. Interview, 1 May 2014.
11. The Guardian ‘Banks put yearly bill for radical reforms at £15bn’, 20 March 2011.
12. Interview, 10 April 2017.
13. Interview, 1 October 2013.
14. Interview, 25 September 2013.
15. Interview, 8 August 2013.
16. Interview, 8 August 2013.
17. Interview, 15 October 2013.
18. Interview, 10 July 2013.
19. Interview, 8 August 2013.
20. Interview, 10 July 2013.
21. Interview, 25 September 2013.
22. Interviews, 18 September 2013 and 15 October 2013.
23. Interview, 3 June 2013.
24. Interview, 16 August 2013.
25. Interview, 28 November 2013.
26. Interview, 28 November 2013. See also Financial Times ‘Osborne grants big banks a concession’, December 19 2011.
27. Interview, 16 August 2013.
28. Interview, 18 September 2013.
29. Interview, 16 August 2013.
30. Interview, 2 October 2013.
31. Interview, 2 October 2013.
32. Interview, 2 October 2013.
33. Interview, 18 September 2013.
34. Interview, 3 June 2014.
35. Interview, 15 October 2013.
36. Interview, 25 September 2013.
37. Interview, 22 May 2014.
38. Interview, 8 August 2013.
39. Interview, 29 May 2014.
40. Interview, 22 May 2015.
41. Financial Times ‘Osborne to press Lloyds on disposal’, 12 April 2011.

Acknowledgements
I am grateful to the 62 officials and practitioners who agreed to be interviewed on an anonymous basis between 2012 and 2014.

Disclosure statement
No potential conflict of interest was reported by the author.

Funding
This research was conducted as part of a two-year project on ‘Policy Networks and Regulatory Reform in the City of London’, supported by the Economic and Social Research Council (Grant Ref ES/K001019/1).

ORCID
Scott James  http://orcid.org/0000-0002-4632-9288

References
Austen-Smith, D. (1993) ‘Information and influence: lobbying for agendas and votes’, American Journal of Political Science 37(3): 799–833.
Bell, S. (2012) ‘The power of ideas: the ideational shaping of the structural power of business’, International Studies Quarterly 56: 661–73.
Bell, S. and Hindmoor, A. (2015), ‘Taming the city? ideas, structural power and the evolution of British banking policy amidst the great financial meltdown’, New Political Economy 20(3): 454–74.
Bernhagen, P. (2007) The Political Power of Business: Structure and Information in Public Policymaking, London: Routledge.
Bernhagen, P. and Bräuning, T. (2005) ‘Structural power and public policy: a signaling model of business lobbying in democratic capitalism’, Political Studies 53(1): 43–64.
Culpepper, P.D. (2015) ‘Structural power and political science in the post-crisis era’, Business and Politics 17(3): 391–409.
Culpepper, P.D. and Reinke, R. (2014) ‘Structural power and bank bailouts in the United Kingdom and the United States’, Politics and Society 42(4): 427–54.
Fairfield, T. (2015) ‘Structural power in comparative political economy: perspectives from policy formulation in Latin America’, Business and Politics 17(3): 411–41.

Farrell, H. and Newman, A.L. (2015) ‘Structuring power: business and authority beyond the nation state’, Business and Politics 17(3): 527–52.

Grossman, G.M. and Helpman, E. (2001) Special Interest Politics, Cambridge, MA: The MIT Press.

Hacker, J.S. and Pierson, P. (2002) ‘Business power and social policy: employers and the formation of the American welfare state’, Politics and Society 30(2): 277–325.

Hay, C. and Rosamond, B. (2002) ‘Globalization, European integration and the discursive construction of economic imperatives’, Journal of European Public Policy 9(2): 147–67.

ICB (2011a) Independent commission on banking: interim report – consultation on reform options, April 2011.

ICB (2011b) Independent commission on banking: final report, September 2011.

Kennan, J. and Wilson, R. 1993. ‘Bargaining with private information’, Journal of Economic Literature 31(1): 45–104.

Lindblom, Charles E. 1977. Politics and Markets, New York: Basic Books.

Przeworski, A. and Wallerstein, M. (1988) ‘Structural dependence of the state on capital’, American Political Science Review 82(1): 11–29.

Smith, M.A. (2000) American Business and Political Power: Public Opinion, Elections, and Democracy, Chicago, IL: University of Chicago Press.

Spence, A.M. (1973) ‘Job market signaling’, Quarterly Journal of Economics 87(3): 355–74.

Streeck, W. and Schmitter, P.C. (eds.) (1985) Private Interest Government, London: Sage.

Swank, D. (1992) ‘Politics and the structural dependence of the state in democratic capitalist nations’, American Political Science Review 86(1): 38–54.

Woll, C. (2014) The Power of Inaction: Bank Bailouts in Comparison, Ithica and London: Cornell University Press.

Young, K. (2015) ‘Not by structure alone: power, prominence, and agency in American finance’, Business and Politics 17(3): 443–72.