

# CHAPTER 3: THE PERNICIOUS EFFECTS OF FOLK MODELS OF ECONOMIC REGULATION

*HOW UBER'S ENTREPRENEURIAL GUERRILLA WARFARE CREATES THE  
REGULATORY DYSTOPIA THEY FEAR*

*KONRAD POSCH*

POLITICAL SCIENCE PH.D. CANDIDATE  
UNIVERSITY OF CALIFORNIA, BERKELEY

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**ABSTRACT:** (WORDS: 1000)

This project focuses on disruptive technological innovations (DTIs), innovations which arise from technological change and disrupt the regulatory regime. Building on Cortez's (2014, 183) concept of regulatory disruption from administrative law, these DTIs disrupt the regulatory regime and elicit a response because they are clearly within an agency's jurisdiction but cannot be addressed by the current regulatory regime. DTIs can disrupt the *operation* of the regulatory regime by changing what is possible within a regulatory domain, often by altering the speed, scale, or complexity of the regulated activity.<sup>1</sup> DTIs can also disrupt the regulatory *paradigm* by challenging regulators' fundamental understanding of their responsibility toward the regulated domain.<sup>2</sup>

Uber is the archetypical disruptive entrepreneur of today. It applies the DTI of IT platform coordination to the ride-hailing sector and explicitly engages in "guerrilla warfare"<sup>3</sup> with labor, consumer protection, and sectoral regulators. Unsurprisingly, Uber's tactics are constant across state and national borders. Surprisingly, they inspire similar hostile responses despite archetypal differences between the regulatory cultures of different states (conservative Texas and liberal California)<sup>4</sup> and between Kagan's (2001) adversarial legalistic USA and cooperative European countries.

To explain this unexpected similarity of response across diverse regulatory contexts, this paper presents three Bayesian process tracing<sup>5</sup> comparative case studies of Uber-regulator interactions in San Francisco, Austin, and Berlin. Uber employed regulatory guerrilla warfare motivated by a fear of regulatory impediments based on a *folk economic model* of regulatory response to DTIs. These cases demonstrate that Uber's guerrilla tactics were *the mechanism that created* the dystopic

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<sup>1</sup> There are surely more mechanisms of disruption. Empirical examples suggest that speed (i.e. high frequency trading, (Lewis 2015) (Ford 2017)), complexity (i.e. Deep Water Horizon oil rig disaster, (Mills and Koliba 2015)), and scale (i.e. cross-national production networks) are three ways technological change disrupts the existing structure of regulatory regimes by changing the practicalities of the regulated activity.

<sup>2</sup> Genetically Modified Organisms (GMOs) in food are an excellent example of such a challenge as they raise the question of whether the products from GM plants are substantially different from those of their non-GM brethren. GMOs past and present will be covered in another chapter of my dissertation

<sup>3</sup> (Lashinsky 2017, 97) aptly dubs Uber's tactics "guerilla warfare." (Collier, Dubal and Carter Forthcoming, 8-9,11-13,18-19) provide an excellent overview and framing of these tactics as an exercise of structural (eg. threat of exit), insider instrumental power (eg. traditional lobbying), and outsider instrumental power (eg. organizing customers to petition regulators or "clicktivism"). Even traditional forms of power were exercised in characteristically more subversive and anti-regulation ways than the might otherwise have been, such as coopting celebrities to shame regulators.

<sup>4</sup> (Tausanovitch and Warshaw 2013) provide empirical measures to ground the common understanding of liberalness and conservativeness of cities and states. As predicted by common understanding, California is as liberal as Texas is conservative. While (Collier, Dubal and Carter Forthcoming, 7-9) separate cities into further types based on metropolitan characteristics which see Austin and San Francisco as similar, their findings demonstrate that such characteristics are not important to outcomes.

<sup>5</sup> (Fairfield and Charman 2017) define a logical Bayesian approach to process tracing which serves to discipline analysis and clarify results.

regulatory impediments that they originally feared. Disruptive entrepreneurs create the dystopia they fear through the myopia of their rhetoric.

DTIs are a subclass of emerging technologies that have moved beyond a *potential* to an *actual* social impact because they are used “in the wild” to shape society thus eliciting a response from society.<sup>6</sup> While built upon Christensen's (1997) concept of disruptive innovation, disruption in this project is observed from the perspective of the regulator and thus focuses on disruption to the *state* rather than to a *market*. Muddling state and market disruption creates entrepreneurial braggadocio that spreads a folk economic model of regulators as an intrinsic impediment to DTIs because it equates changing the market with changing the world.

By a folk model I mean a “statement of the common-sense understandings that people use in ordinary life [rather than] various “specialized” and “scientific” models.”<sup>7</sup> By unpacking the folk economic model of the regulatory response to DTIs, this paper demonstrates that while it *seems* obvious to many entrepreneurs that regulators are an impediment to innovation, it is *just one possible relationship* between regulators, entrepreneurs, and innovation which is empirically observable and theoretically explainable. Quieter models of success are also theoretically conceivable and empirically observable.<sup>8</sup>

Failure is loud, success is quiet. Regulatory failures like the Deepwater Horizon oil spill and 2008 Global Financial Crisis are loudly publicized. Much quieter are regulatory responses which are something other than failure like American recombinant DNA regulation following the 1975 Asilomar Conference.<sup>9</sup> This mismatch reinforces a folk understanding of regulators as destined to fail. Worse yet, loud proclamations of inept regulators’ inevitable failure often create failures when alternative rhetoric could avoid them.

Regulatory scholars in political science and law know the folk economic model as “capture” within a “command and control” regulatory structure. These scholars who study actually existing regulation have repeatedly demonstrated that such catch-all models of regulation are deceptively inadequate.<sup>10</sup> From a legal perspective, Malloy (2010) provides an excellent overview

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<sup>6</sup> You can think of this as a permutation of Polanyi’s (1957 [1944], 76) double movement in that this response does not require agency but is the natural result of the changes brought by disruptive innovation. In other words, an emerging technology becomes a DTI when it elicits a social response beyond merely anticipatory governance due to effects experienced by a portion of society in their everyday lives.

<sup>7</sup> (D’Andrade 1987, 113)

<sup>8</sup> Such quiet successes include beneficial constraints such as the 1975 Asilomar Conference’s recommendations for recombinant DNA regulation which formed the basis for the 1976 official US guidelines (Berg 2008, 290) and the US and EU mandate to adopt electronic health records (EHR). Both are explored in my dissertation.

<sup>9</sup> (Berg 2008)

<sup>10</sup> (Slayton and Clark-Ginsberg 2018) is a good recent review of the inadequacy of the capture model. But frankly, opening any issue of any journal with “Regulation” in the title (c.f. Regulation & Governance) would tacitly demonstrate this point. This includes, ironically, Regulation magazine published by the Cato

of two alternative social constructions of command and control regulation. Nevertheless, scholars who *do not* study regulation still draw upon capture as the baseline against which all work on regulation is judged.

In other work, I develop a full deductive typology of regulatory responses to DTIs by generalizing the variables which underlie the folk economic model.<sup>11</sup> The typology builds on the observation that the folk understanding of Stigler's fixed concepts in "The Theory of Economic Regulation" (1971) should more properly be understood as values of variables in light of the alternative understanding of regulation in Streeck's "Beneficial Constraints: On the Economic Limits of Rational Voluntarism" (1997). That typology paper places Stigler's original theory in conversation with Streeck's and generalizes common concepts into five constitutive variables (relationship, access, impetus, outcomes, and effect)<sup>12</sup> which are then used to deductively define a typology of seven distinct models that describe regulators respond to DTIs. This seven model regulatory response typology establishes a broader understanding of the effects regulators can have on innovation spanning from impediment to driver of adoption.

It has become cliché to note the speed of technological change and lament the inability of social and legal institutions to keep up. One phalanx of this narrative brandishes the word "disrupt" to storm the halls of stodgy industries and regulatory agencies intent on dismantling them. Yet despite this modern narrative of disruption, significant technological change is not the invention of the past year, decade or generation. Despite libertarian narratives which prompt disruptive entrepreneurs to use regulation as the foulest profanity to decry state inadequacy, regulators have adapted to technological change each time it arose. Although sometimes inadequate and never perfect, these adaptations invariably happened.

This paper presents three city case studies that demonstrate that Uber employed "guerrilla warfare" against regulators because Uber understood regulators within a folk economic model that declares regulators to be inherently unable to foster innovation. These cases span states, countries, and continents to demonstrate the cross-context perniciousness of Uber's folk economic model of regulators as the inherent enemy of innovators.

Uber's folk economic model absurdly upsets regulators, elicits a harsh response, and then points to regulators' harshness as proof that regulators are an impediment to innovation. History shows that regulators *can* be a challenge to disruptive innovation. However, Uber's contemporary experience demonstrates that if entrepreneurs selectively extrapolate history to a folk model that

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Institute (and AEI before 1989) which has found 31 years of intricacy on regulatory issues to write about since July 1977 despite their libertarian ideology.

<sup>11</sup> (Posch 2018) and the theoretical core of my dissertation.

<sup>12</sup> Malloy's (2010) "conventional construction" is consistent with Stigler's economic model understanding while his "alternative construction" is the definition of a regulatory politics model to describe the variations in the command and control form of regulation. Indeed, his three propositions of "rigidity", "homogeneity", and "competency" helped me define my variables of effect, outcomes, and access.

says regulators *must* be a challenge, then they will *create* the very challenge they fear. Regulators can be allies of innovators only if entrepreneurs look past the myopia of entrepreneurial rhetoric.

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