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Business Risk Management Practices: The Influence of State Regulatory Agencies and Non-State Sources

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Business Risk Management Practices

The Influence of State Regulatory Agencies and Non-State Sources

Bridget M. Hutter and Clive J. Jones¹

Abstract

The influence of external organizations and pressures on business risk management practices has hitherto been examined through the influence of state regulatory regimes on businesses. This literature concentrates on key socio-legal concerns about the influence of the law in social and economic life (Heimer 1996) which is an important source of information about business risk management practices. However most of this work does not clearly differentiate the importance of state regulatory regimes relative to other external pressures on business. We know that the sources of regulation and risk management are diversifying, as are the tools and techniques employed to manage and regulate risks. What we do *not* have is much empirically informed research about the range of sources influencing the business world and in particular the weighting of influence exercised by them. 812

regulation. This literature identifies factors which may encourage or limit the role of the law as a risk management tool – although se12 436.371e03371.00141 Tw 12 0 0320. 12284441 74

The term civil society embraces a fairly broad range of actors and organizations (Hutter and O'Mahony 2004). Accordingly the range of sources of regulation in the civil sector is diverse. Perhaps the best-known regulatory sources in this sector are NGOs, a category which itself includes a diverse range of organizations which may operate at the local, national or international levels. Also important in the civil sector are standards organizations which produce standards about product quality, quality assurance, and risk management (Brunsson & Jacobsson 2000) and professional organizations which have long played a very important regulatory role in regulating entry conditions to the professions and laying down standards of conduct. Again the influence of civil society sources on state regulation has been discussed but what is now needed is more empirical information on the influence of civil society on risk management practices. Standard setting agencies clearly have the capacity to set industry and product standards and thus have a very direct influence on business. NGOs and professional representatives may also have influence either directly as part of the business decision-making apparatus or indirectly from outside the business.

These organizations may influence regulati

some of those we spoke to this is a nonsensical question which will reap very obvious responses, namely that if something is a matter of law then it is known about and complied with – ‘food safety hazards must be controlled by law by the business, therefore these are not options’. Others disputed this. They believed that not everyone does know or understand the law and they saw one of the major challenges of regulation being to attain and maintain comp

Table 1: The range of influences upon managers when considering food safety and food hygiene risks based on the statistical mean of all questionnaires (completed) by managers.

Source of influence – ranked by level of influence	Influence	Influence index (Mean values of questionnaires)
EHO	Most influence	1.35
Consumers		1.36
FSA		1.74
TSO		1.90

This said one of the surprising findings of the survey is that with one exception (1 out of 15 respondents) none of the micro size catering businesses proactively sought advice from EHOs. This is especially surprising as EHOs emerged as an important source of information for other food businesses. Two-thirds of the businesses we surveyed actively seek advice from the EHO. Inspection appears to be an important educative channel and it may be that micro businesses find these visits especially helpful – thus the perception that they have a good relationship – yet they may simultaneously lack the confidence to actively ask EHOs for advice in the way larger businesses do.

The other local authority regulators we questioned respondents about were TSOs. They are clearly of influence (62%) on our food businesses but not as strong an influence as EHOs (91%). Knowledge about TSOs was patchier than was evident in the case of EHOs. For example when asked about TSOs 52% of micro and small businesses indicated a response of ‘Not applicable’ or ‘Don’t know’ compared to 10% who did not or could not respond on the subject of EHOs. Little patterning was evident according to the size of business or whether the business was a retail or catering business. TSOs received almost no spontaneous mention elsewhere in the survey where they were mentioned by less than 2% of respondents. This would suggest that an awareness exists of trading standards matters but managers, directors and owners have had little experience of direct contact with a TSO⁷.

Food Standards Agency

During the first phase of research the role of the FSA was, as one might expect from this group of experts, well known. There was a great deal of uncertainty in the first phase about how well known the FSA would be within the food industry. Yet in our second phase survey the FSA was ranked as the third most important external influence on food retail and catering businesses. This ranking did vary between businesses. For example, almost two-thirds of managers from a large take-away chain did not indicate that the FSA had any influence upon them by either ticking ‘Not applicable’ or not responding to the question. This response was consistent with most of the other responses regarding external regulators from this company – they were characterized by a medium to high proportion of ‘not applicable’ or non response to questions on this topic.

In comparison, 90% of managers of a medium-sized catering chain claimed the FSA as their strongest influence – more than the influence of EHO (80%). We suspect that this finding should be treated with caution as their managers did not reference the FSA elsewhere in their responses.⁸ Further evidence of confusion is that the retail manager reported that his branch had been audited by the FSA.

⁷Business managers that only ever worked in Greater London would not have contact with a local government enforcement official who was a dedicated TSO; functionally such an enm 8035 Tm(97.971e0.02)Tj10.02 0 Ou.075

At a basic level there did seem

responded to a question about their understandings of consumer concerns. In two companies 100% of managers thought that consumers rated food safety and food hygiene issues as ‘Very important’ and in these two companies ‘Labelling and product description’ was seen to be the second highest concern to consumers. Overall ‘Price’ (value for money) was cited as the second highest concern of consumers.

Table 2: The range of perception importance to consumers by managers when considering a range of food attributes commonly related to risk based on the statistical mean of all questionnaires (completed) by managers.

Consumer concerns	Managers understandings of relative importance of consumer concerns	Importance index (Mean values of questionnaires)
Food safety and hygiene	Most important	1.1
Price (value for money)		1.65

During the period of study it was known that some businesses in the sample had first-hand experience of direct media attention in the form of the 'undercover investigative television reporter' genre. But specific details were difficult to obtain through the survey. Respondents were however more prepared to discuss the more *diffuse effects of the media*. A small group of individual managers across the samp

about moral hazard problems – ‘Insurance is the enemy of the good as it is designed to average out loss resulting in the good not being rewarded and the bad not being punished’ (interview respondent). More generally the extent to which insurance does play a role in promoting food safety and food hygiene is unknown.

Some 60% of managers of micro/small businesses compared to 50% of medium and large companies¹⁰ claimed to have insurance cover for food hygiene and food safety incidents. Conversely, micro and small business managers (30%) view insurance companies as much less influential than did managers of medium and large businesses (50%). Aside from insurance cover 20% of all managers received information on food hygiene and food safety from their insurance company but only one business (a micro/small business) reported ever having been inspected by an insurance company.

Our survey found that 15% of managers in medium- and large-size businesses regarded insurance companies as having a ‘strong influence’ with the medium and large catering businesses being more inclined to regard them as strongly influential (20%) than the retail only businesses (8%).

Lawyers

The relevance of lawyers to risk management was not well understood by our survey respondents. Lawyers were in fact considered to have the least influence of all the external actors we asked about in the survey. A slight difference in influence does emerge between the catering and retail sectors with the former responding that lawyers have greater influence than was the case with the retail sector.¹¹ Interestingly almost 90% of managers of micro/small businesses did not answer this question.

Only two managers from phase 1 spontaneously referred to any legal influence upon food safety. This was less a comment specifically regarding lawyers as individuals and more a comment on how the legal system in its broadest sense was perceived to operate. A director of a catering company commented that their risk management approach had a bias towards viewing risk from a legal perspective in an attempt to avoid litigation possibly relating to their business operations in the United States. A senior risk manager from the headquarters of a large licensed catering chain commented on the rise in claims from customers who had ‘fallen over in the car park after leaving our establishments’. He considered this an example ‘compensation culture’. Surprisingly, given the debates about the UK being riddled with a ‘compensation culture’ his was the only explicit mention of this phenomenon in phase 1 and phase 2 of the research. Regardless of accuracy we expected these claims to be reflected in our findings but it was far from the case.

¹⁰ Some 33% of directors/senior managers responded with ‘don’t know’.

¹¹ The ‘no influence’ responses were particularly high amongst managers of a supermarket chain (49% replied that lawyers had ‘no influence’ when considering food hygiene and food safety risks). However over a third of respondents in three (two large and one medium) of the hospitality chains we surveyed did consider lawyers a ‘strong influence’ or of ‘some influence’.

Pressure groups/NGOs

Pressure groups, especially NGOs, are perhaps one of the most well known regulatory sources in the civil sector. They are especially important for their information-gathering

business in either the retail or catering sectors represented in the sample used a consultancy as their main source of information about food safety and hygiene risks.

Not all consultancies were viewed positively and some received a great deal of criticism from all of the sectors represented. They were seen to be exploiting the confusion of micro firms and SMEs relating to HACCP¹² – ‘consultants are making a killing out of HACCP, just pulling stuff off the net and then selling it’ (interview respondent). But there was more than moral indignation, some expressed concern that there is ‘over-implementation of risk management practices due to the advice of commercial consultants’. This very much chimes with evidence that consultancy firms

Of the micro, small- or medium-sized businesses only one indicated membership of two trade associations (White mentioned the Soil Association and a ‘Small Business association’). No trade association that one would expect to find such as the Institute of Directors, British Chambers of Commerce or Federation of Small Business was mentioned.

Some 5% of managers for medium and large businesses indicated that a trade association made checks on food safety and food hygiene on their premises. A similar figure indicated that a trade association provided information on food safety and food hygiene to them and 2% indicated this information was provided to their staff. None of these managers named or described these trade associations. It is thought that confusion exists with categories of organization – some managers may believe that a commercial consultancy is a trade organization. Similarly, some managers who mentioned using the services of a commercial consultancy may in fact be the clients of the commercial arm of a trade association. The line between the two is often unclear.

When considering food safety and food hygiene risks directors of large retail businesses were moderately more influenced by an ‘industry association’ than the directors of large catering business although in both sectors the influence is not ‘strong’.

Some participants were very supportive of *self-regulatory schemes* such as the Little Red Tractor launched in the UK in June 2000 by Assured Food Standards which was created by the National Farmers Union (NFU) with government backing (Meat and Livestock Commission).

Other participants preferred greater clarity about whether or not there is a regulatory requirement upon them or not i.e. a legal requirement to comply. There was a view that if schemes such as these are to have any chance of success then strong enforcement is necessary.

Several references were made by managers in the survey to what we believe are in-house schemes or proprietary standards which do not appear to have been created by trade associations or state regulators. Such schemes and standards have either been developed internally within businesses or have been introduced with the assistance of paid external technical or business consultants. These schemes and standards were referred to in passing by several of the managers using an acronym: all of whom worked for the large businesses in the sample. Adherence to these schemes and standards appeared to be mandatory for those working within the business.

One area where our understanding of risk management is not entirely clear is where managers interact with experts from outside their branches. What is obvious is that some of managers in the sample are unsure of the precise identity of the experts they encounter in the course of their work – are they EHOs, consultants, or specialist company staff? When one considers the operational outcome of the combination and

evidence for UK retailers and brand owners to demonstrate “due diligence” in the face of potential prosecution by the enforcement authorities’.

This publication has now become an international mark of excellence. Certification to the Standard verifies technical competence and aids manufacturers, brand owners and retailers fulfilment of legal obligations. It also safeguards the consumer.’ http://www.brc.org.uk/standards/about_food.htm 2006

(possibly contradictory) interaction of the various sources of influence outlined above one would not be surprised if some confusion as to ‘what is what’ and ‘who is who’ were to result amongst managers and staff.

Discussion

Knowledge of state regulation

One of the strong messages drawn from the research is that state regulation remains a key influence on business risk management practices despite some confusion at store level about state regulatory arrangements. Knowledge of EHOs, the local authority regulators, was most widespread and most sophisticated. This is not entirely surprising as they are in most contact with the industry at floor level and their remit directly relates to the food safety and food hygiene risks we asked about. TSOs do not work directly to this remit but the survey responses do not seem to have such a nuanced reason for their ignorance – the indications are that they have less knowledge of trading standards. Knowledge of the nationally-based FSA is high at senior management and policy levels of large businesses but less so at junior management level. Overall, however, knowledge of the FSA amongst businesses was much higher than our expert group anticipated it would be.

The confusion about the specificities of the overall regulatory system echoes the findings of other studies, although the general levels of knowledge of EHOs appear to be higher than those found by studies of other regulators. Genn (1993) and Brittan (1984) found great variation in levels of regulatory knowledge in their studies, with confusion about regulators highest on the smaller sites they visited. Genn also found little evidence of the regulated in smaller businesses being prepared to debate with inspectors, rather like the SMEs in this study. In larger companies there is a greater readiness to use regulators as a resource. In Hutter’s (2001) study of a national railway company the social dimensions of regulatory knowledge and understanding were striking with senior personnel having a much greater understanding of the regulatory system than those lower down the hierarchy. This of course very much accords with our findings.

The literature on the impact of state regulators reveals a variable impact. The overwhelming majority of railway employees interviewed in Hutter’s 2001 study thought that the state regulator was very important in bringing about higher standards of health and safety in the industry. Likewise Gunningham, Kagan and Thornton (2003) conclude that regulation does matter in shaping corporate behaviour. This contrasts with earlier studies by Gricar (1983) and Clay (1984) on OSHA (Occupational Safety and Health Administration) inspectors in the United States. Most studies argue for the necessity of maintaining some kind of outside policing of business risk management primarily to ensure that risk management objectives are established and maintained on a firm’s agenda (Gunningham and Grabosky 1998; Hutter 2001) and there is a need for ‘credible enforcement’ (Gray and Scholz 1991; Gunningham 2002).

Knowledge of non-state influences

Respondents readily understood that there are other non-state external influences on their risk management practices although our survey found that generally these are less influential than the state regulators. The influence of non-state bodies was best understood by our senior experts and policy makers who spontaneously referred to a wide range of such influences. Our survey revealed knowledge of these influences and also presented us with some surprising results. For example, the role of consumers as an important influence on business risk management practices was not flagged up by our experts yet in our survey consumers were cited as one of the strongest influences on risk management. Indeed, not only did consumers figure highly as an influence they were also deemed to rank food safety and food hygiene as the most important consumer concerns.

Interestingly, the influence of the media was deemed to be well below consumers and state officials and the other main sources of civil influence. NGOs, surprisingly, were not well understood as an influence despite their large role in opposing GM foods and promoting organic produce. We had expected a greater knowledge of them and that they would be attributed a more prominent regulatory role. Another surprise is the fairly low influence attributed to lawyers. Given the prominent debate about the compensation culture respondents rarely mentioned the possibility of compensation claims or civil actions.

Likewise insurance companies also appeared to have a much less influential role than attributed by some commentators. However, the converse was true for other types of service company, namely private consultancy firms. These appear to have influence and, in fact, the potential for substantial influence in some areas of the industry. The nature of this influence is

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(1994), for example, argues that preferential buying or consumer boycotts may have the capacity to influence business environmental behaviour more than state regulation. But there is no corresponding research in the area of food safety and food hygiene. A study in the UK found consumers regard food safety as highly important but that they have few concerns about it as they generally agree that standards in the UK are very high (IGD 1998).

The role of broader social concerns in influencing business has been discussed. The

found to be non-compliant by an enforcer rather than advice requested from a regulator at the initiation of the businesses and therefore unrelated to an inspection (cf Fairman & Yapp 2004; Hutter 1988). One reason for SME reliance on state systems is that many small businesses have less contact with non-state sources which provide information and advice. They are neither members of trade or business associations which may provide updates or even training on food safety and food hygiene matters nor do they use consultancies (Fairman and Yapp 2004; Genn 1993). This of course contrasts with large businesses which have greater regulatory capacity of their own and more likely to belong to associations, employ consultancies and take out insurance cover.

A second factor which may be relevant in

work which calls for a mix of regulation sources (Eisner 2004; Gunningham and Grabosky 1998). This work recognizes that the state has an important role to play but that it also has its limitations which may be mitigated by other influences beyond the state. The mix may be a formalized one, for example enforced self-regulation (Braithwaite 1982; Coglianese and Lazer 2003; Hutter 2001). Alternatively, there may be a more loosely coupled arrangement where the state relies on organizations beyond the state to manage risks or where there are multiple influences acting independently of one another (Hutter 2006). Certainly, the research suggests that economic and civil sector influences are of equal importance.

These findings suggest that in Hood et al.'s (2001) terms the state, consumers, and consultancies, have a direct influence on business risk management practices. The media, lawyers, insurance companies and NGOs are more properly understood as part of the context, that is, as background influences albeit with the capacity to move from the background context to be part of the content. The state's influence is probably the best understood direct influence on business risk management. The role of consumers is less well understood and there is very little at all on the influence of consultancies. These influences do seem to work in mysterious ways and differentially according to the social structure of the business. They certainly warrant more research and investigation as to the nature of their effects. We should not automatically assume, for example, that all consultancies have a positive influence on risk management practices. Certainly, they have been implicated in regulatory creep.

The background influences are of course variable according to topicality and size of business. The ways in which factors play out and interact are not well understood; in fact there is a surprising lack of information on these issues. The academic literature does suggest that each of the background influences has the potential to be a direct influence but as yet we need a great deal more evidence of this and how it might be realized and the conditions under which each influence is likely to be helpful. The influence of insurance companies is an area which particularly deserves greater scrutiny.

We do know that businesses are subject to a complexity of pressures on their risk management practices. Some are external to their organization and others are within their organizational boundaries. We have concentrated in particular upon positive influences which encourage risk management but there are negative influences too. Indeed different pressures may be in tension. As Gunningham, Kagan and Thornton (2003) point out, the nature of these interactions is not well understood and the next step is to explore this further. This paper draws on research undertaken with the food industry. Our next step is to compare this with another risk regulation domain to better understand how the various external influences on business risk management might work across different areas.

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