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Revolving Doors - We Got It Backwards

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REVOLVING DOORS - WE GOT IT BACKWARDS

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I. INTRODUCTION

"Eric Ben-Artzi is a brave man. The former Deutsche Bank risk officer was one of three whistleblowers who reported improper accounting at the German bank to regulators in 2010 and 2011. In 2015, the US Securities and Exchange Commission imposed a $55 million fine against the bank over the issue. Ben-Artzi is due a share of 15% of this sum, adding up to $8.25 million. In an opinion piece in the Financial Times on Thursday, he revealed that he had rejected the payout. . . . In his piece, Ben-Artzi really homes in on two hot-button issues that get a lot of people on Wall Street uncomfortable: the revolving door between Wall Street and regulators, and the regulators' propensity to fine the firm, rather than the individual. On the first issue, he details the numerous Deutsche Bank lawyers who moved to and from the firm and the SEC. This is common on Wall Street, and it is something that the Federal Reserve for one has sought to address. For example, bank supervisors at the Fed can't join a bank that they had been supervising for a year after leaving. Still, the relationship between Wall Street banks and the regulators supervising them continues to be a focus..."[1]

The revolving door phenomenon in the financial markets, in which senior public officials transfer from the public service to the private sector after finishing their term as public officials, and vice versa, is widespread.[2] This gives rise to concern of regulatory capture, which happens when the regulators respond, via regulations, to the wishes of

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1. Matt Turner, *A Deutsche Bank Whistleblower Just Pulled a Gutsy Move to Highlight What's Wrong with Wall Street*, BUS. INSIDER, Aug. 18, 2016.

2. Just to mention a very limited list in the US financial market, Alan Greenspan who served as chair of the Federal Reserve became an advisor for hedge fund Paulson & Co. after leaving the Fed., Richard Walker, Deutsche bank's longtime general counsel (who recently left the bank) was once head of enforcement at the SEC, Lawrence Summers, who, while serving as Treasury Secretary, pressed for deregulating the financial markets then moved to D.E Shaw hedge fund and many more.

strong interest groups (also known as pressure groups), such as the regulated industry, instead of protecting the interests of the general public.[3]

To overcome this problem, many countries have enacted laws that try to reduce the industry's ability to capture the regulator. One of the most common methods to combat regulatory capture is through mandatory cooling-off periods for senior officials, which are often required by conflict of interest rules.[4] A cooling-off period is basically a limited period of time in which a public official is precluded from working for those parts of the private sector with which he had contact during the time he was in office.

The underlying logic is that the passage of time will create a buffer between the (former) regulator and his previous job as a civil servant, weaken his connections with his former employees and co-workers, and neutralize his ability to affect their decisions. This, the thinking goes, would make the regulator less desirable to the regulated firms ex-post, and thus reduce his exposure to pressure by the industry ex-ante, i.e during his term as a regulator.[5] This is also the reason cooling-off periods, usually one to two years, are widely used around the world, including in the United States. In fact, the U.S. and a few other countries have also demanded a cooling-off period for the other side of the revolving door, namely, for people joining the public sector after working in the private sector. Typically, such cooling-off periods preclude the newly-hired public officials from handling any issues related to their previous job and/or employer for a few months or years.[6]

This Article proposes that although revolving doors do incur some costs, they also offer certain benefits, and might, if designed correctly, increase the quality of supervision. The main argument of this Article is that due to specific behavioral biases such as the *Availability* bias and the *Lock-In* bias, combined with office socialization processes that occur while the individual serves as a public official, regulators who

3. MARVER BERNSTEIN, REGULATING BUSINESS BY INDEPENDENT COMMISSION (1955); George Stigler, *The Theory of Economic Regulation*, 2 BELL J. ECON. & MGMT. SCI. 3, 3–21 (1971); Sam Peltzman, *Toward a More General Theory of Regulation*, 19 J. L. & ECON. 211, 211 (1976).

4. For example: 18 U.S.C. § 207 (2018) which restricts federal employees in the executive branch of government in performing certain activities for private parties post-employment with the government.

5. It is important to note that even though this article chooses to focus on revolving doors in the financial markets and the cooling-off periods designed to reduce or prevent regulatory capture in this market, it is not at all unique to the financial sector and is, in fact, a mechanism which is used in many other sectors as well.

6. See for example the instructions that President Obama issued on January 21, 2009, when he came into office – Exec. Order No. 13490, 74 Fed. Reg. 4673 (Jan. 21, 2009).

join the private sector tend to comply more with regulatory instructions issued by their previous colleagues than other senior executives. That is because, at least in their first few months after leaving public office, they still identify strongly with the staff of the regulatory body for which they used to work.

Additionally, this Article argues that the possibility of moving from the public sector to the private sector increases the chances that regulatory institutions will hire top experts for relatively low pay. Obviously, this improves the quality of the regulatory work and the resulting regulation. Where the ability to transfer from the public sector to the private sector is curtailed, the quality of regulation will decline and this would, eventually, undermine the overall public welfare that the regulation seeks to promote.

This Article does not intend to argue that every regulator is subject to socialization processes and behavioral biases to an extent that influences his or her behavior. Nor does this Article attempt to establish that these processes are the dominant incentives for regulators in every regulatory setting. The thesis of this Article is that socialization processes and behavioral biases may affect regulatory behaviour in a way that contradicts the classic capture theory. This possibility has gone, so far, almost unnoticed. A future line of research will be necessary to empirically test this theory and to identify the specific regulatory settings where these incentives are more likely to be acted upon and influence regulatory behavior.

It is a popular belief that moving from the public sector to the private sector is an opportunistic, negative act, while moving from the private sector to the public sector is seen as desirable and even altruistic. This paper sheds light on the less-discussed problems lurking on the other side of the revolving door: moving from the private sector to the public sector. These problems result from the behavioral biases and socialization processes mentioned above, and which have a lingering effect on the regulators' performance abilities as civil servants. It is these processes that make it easier for the regulators to be unwittingly captured and create an opening for the regulated industry to affect the due process of regulation.

II. THE NEED FOR AND COSTS OF FINANCIAL REGULATION

Financial markets have special attributes that require regulatory intervention. They are complex markets that are abundant with externalities, asymmetric information, moral hazard, and agency problems.[7] These markets bring together sellers and buyers of financial instruments where price discovery is established. The price of the traded instrument is determined, like the price of any other product in regular non-financial markets—by the supply and demand curve.[8] However, unlike non-financial products or goods, financial instruments have a special trait: the benefits that they confer are largely unknown, as the underlying product has a prospect of earnings in the unknown future. Therefore, their value is based on the prediction of the traders in the market with respect to the future cashflows and appreciation of the financial instrument over time.[9] Price discovery is one of the core functions of financial markets, providing information about investors' belief with regard to the future price of the assets sold on the market.[10] The price of the financial instrument should reflect the present value of the distribution of prices at the date on which the investor expects to sell the instrument plus the sum of the present value of the stream of future cashflows. To accurately price the financial instruments, investors need to have all relevant information about the asset and about the firm marketing it. Financial regulators provide information to the market, mainly through the vehicle of disclosure requirements, which in turn helps the market assign the right price tag to the products sold.[11]

Furthermore, in the financial markets, some products mature over a long period of time, causing a need for regulatory monitoring that is exacerbated by consumer demand for regulation and economies of scale in monitoring. Moreover, the financial firms in these markets are crucially important, from a systemic point of view, to the health of the economy in general. Systemic risk is increased by links and interdependencies, where the failure of a single entity or cluster of entities can cause a cascading failure. This risk needs to be mitigated by regulatory requirements demanding firms to internalize their costs.

For all these reasons, financial regulation is crucial. However, it is also costly. The costs of financial regulation may often prevent the market from reaching an optimum.[12] These costs include costs of regulatory mistakes, systemic risk caused by financial regulation,[13] distortion of competition, costs of fragmentation of the regulatory

7. HADAR Y. JABOTINSKY, FINANCIAL REGULATION IN ENCYCLOPEDIA OF LAW AND ECONOMICS (2017).

8. JOHN ARMOUR, ET AL., PRINCIPLES OF FINANCIAL REGULATION 101 (2016).

9. *Id.* at 101.

10. *Id.*

11. JABOTINSKY, *supra* note 7.

12. *Id.*

13. Roberta Romano, *For Diversity in the International Regulation of Financial Institutions: Critiquing and Recalibrating the Basel Architecture*, 31 YALE J. REG. 1, 1 (2014).

regime,[14] and regulatory capture.

III. REGULATORY CAPTURE

The traditional approach to regulation, the "public interest approach", refers to regulators as public servants who make policy determinations according to their perception of what the public wants.[15] Under this approach, if regulators happen to favor the regulated industry in exercising their regulatory power, it would be due to their belief that this is in line with the public interest.[16] The idea of a captured regulator contradicts this approach.

The issue of a captured regulator who oversees the industry in a lenient way is not a new phenomenon and has been broadly discussed by the literature for many years.[17] According to the literature, a captured regulator will tend to be less vigilant when supervising the industry and will act according to the interests of the regulated firms rather than in accordance with its mandate: to promote the public's welfare. This is known as the "private interest" theory of regulation, which describes the regulatory process as a competition between two interest groups. Under the private interest theory, the regulated industry is well organized and coordinated and is therefore able to extract rents at the expense of the public, which is more dispersed and less informed.[18]

Under this theory, the strong, organized industry is able to capture the regulator and influence decisions in a way which promotes the interests of the regulated firms. This theory takes into account the fact that regulation has broad distributive ramifications: it affects the division of wealth within the society and usually increases the costs to the regulated firms by disrupting them from operating freely in the market in a way which would have maximized their profits. If the regulation is successful, it will cause the regulated firms to internalize their costs. Therefore, it is not surprising that different pressure groups try and influence the regulator in order to minimize the respective harm they would incur from the regulation. [19] If the pressure group is successful, it will capture the regulator—the regulator will promote the

14. Hadar Y. Jabotinsky, *The Federal Structure of Financial Supervision: A Story of Information-Flow*, 22 STAN. J.L. BUS. & FIN. 54 (2017).

15. Michael E. Levine & Jennifer Forrence, *Regulatory Capture, Public Interest, and the Public Agenda: Toward a Synthesis*, 6. J.L. ECON. & ORG. 167, 168–69 (1990).

16. Steven P. Croley, *Public Interested Regulation*, 28 FLA. ST. U. L. REV. 7, 28–31 (2000).

17. *See* Bernstein, *supra* note 3; Stigler, *supra* note 3; Peltzman, *supra* note 3.

18. *Id.*

19. Gary S. Becker, *A Theory of Competition Among Pressure Groups for Political Influence*, 98 Q. J. ECON. 371 (1983).

interests of the pressure group rather than that of the general public.[20]

It should be noted that there are several ways in which the industry is able to capture its regulator.[21] One way is intuitive—the pressure group influences the regulatory work by putting direct pressure on the regulator to change or cancel regulations. Under this framework, the pressure group makes sure to keep close connections with the legislators and regulators in the market, to contribute to political campaigns through political action committees ("PACs"), for example, and to organize fundraisers for politicians. All this is done with the intent of being able to influence the politician or regulator once she goes into office. As one op-ed noted, "It's hard to adopt the Conan the Barbarian approach when you know that the boss of the folks you're talking to is hosting a big fundraising dinner for your ultimate bosses in Congress and the White House."[22]

In addition, the industry might implicitly suggest that it will hire the regulator once her term in office is over. If the regulator is aware of the fact that there is a high likelihood she will be employed by the regulated industry, this might cause her to act with caution and minimize the harm to the regulated industry in her role as a regulator. This might sometimes come at the expense of the public's interest.[23] If the regulator starts looking for her next job while she is still in office, she might be inclined to provide the industry with benefits, such as aiding a specific regulated firm to win a bid that is under her supervisory responsibility, demanding less stringent conditions from the industry with regard to approving and signing agreements, or giving the industry a reduction in fees.

A second way in which the regulator might be captured relates to the fact that the regulated financial industry is usually better organized and better financed than the general public or other groups active in the regulatory sphere (such as consumer NGOs). The problem is rooted in the fact that the financial firms usually have the resources to hire the best experts in the field in order to try and tilt the regulatory decisions in their favor. Moreover, it is very easy for a regulated firm to locate other regulated firms with similar interests and to cooperate with them in communicating with the regulator. This is not the case for consumers who face severe coordination problems that are coupled

20. MANCUR OLSON, THE LOGIC OF COLLECTIVE ACTION (1965).

21. See Becker, *supra* note19; Olson, *supra* note20; Bernstein, *supra* note 3; Stigler, *supra* note 3; Peltzman, *supra* note 3.

22. Megan McArdel, *It's Normal for Regulators to Get Captured*, BLOOMBERG OPINION (Oct. 1, 2014, 11:42 AM), https://www.bloomberg.com/opinion/articles/2014-09-30/it-s-normal-for-regulators-to-get-captured.

23. Jeffrey E. Cohen, *The dynamics of the "revolving door" on the FCC*, 30 AM. J. POL. SCI. 689, 689–708 (1986).

with lack of funding and inability to locate all other consumers affected by the regulation. It is, therefore, only natural that the regulated firms will present more convincing arguments to the regulators. In such an unbalanced situation, the industry captures the regulator and the regulator will promote decisions that benefit the industry instead of regulating to promote the public welfare.[24] In addition, regulators usually shy away from negative public opinions, especially in the media. The worst negative feedback usually comes from the organized industry and not from the general public. Therefore, regulators are sometimes tempted to compromise on less strict regulation in return for peace and quiet.

A third way in which a regulator might find herself captured relates to the fact that the financial industry is a repeat player. During the day-to-day regulatory work, the regulator learns to trust the discretion of the experts who work for the financial firms. Thus, the regulator might forget that these experts are examining the regulatory issue through the lens of being employed by the supervised firms. When the regulator relies heavily on experts, decisions could be made solely based on their expert opinion without question. In this case, the regulator becomes unknowingly captured.[25] Furthermore, the regulator receives the information from the regulated industry. Thus, the information that the regulators receive is always biased toward the perspective of the regulated industry. In addition, the regulators often only get what they ask for, which is not always the same information that they need to effectively regulate.

The "New Governance" phenomenon,[26] in which the industry plays an active role in formulating the regulation by participating in legislative committees, meeting and holding regular discussions with the regulators, and proposing regulatory amendments, intensifies the problem because it increases the interaction between the regulator and the regulated firms. This leads to a situation in which, often times, the regulator is required by law to consult with the industry prior to or during the process of her work. The greater the interaction between the regulator and the regulated industry, the more likely the industry is to capture the regulator, whether wittingly or otherwise.

In an attempt to limit the possibilities for financial firms to openly capture their regulator by promising future benefits, various

24. *See* Becker, *supra* note19.

25. Daniel C. L. Hardy, *Regulatory Capture in Banking* 4 (Int'l Monetary Fund, Working Paper No. 06, Vol. 34, 2006).

26. Roderick A. W. Rhodes, *The New Governance: Governing without Government*, 44 POL. STUD. 652 (1996); Lisa B. Bingham et al., *The New Governance: Practices and Processes for Stakeholder and Citizen Participation in the Work of Government*, 65 PUB. ADMIN. REV. 547 (2005).

researchers have pointed their fingers at the "revolving door" phenomenon. The basic idea is that this phenomenon increases the industry's ability to capture the regulator. Many scholars assume that if we rule out or reduce the revolving door phenomenon, we will also significantly reduce the industry's ability to capture the regulator because it will not be able to promise her benefits like senior jobs within the industry once her term as a regulator is over. One proposed way to limit the revolving door phenomenon is by enforcing cooling-off periods, in which the regulator may not work for any entity that she has previously overseen. The length of cooling-off periods varies from country to country and sometimes even from sector to sector.

IV. REVOLVING DOORS – ANCILLARY PROBLEMS, EXISTING SOLUTIONS

> Under the influence of the capture narrative, the risk of capture has become the dominant concern about the revolving door. The potentially debilitating role of the revolving door was highlighted by Mary Schapiro during her Senate confirmation hearing, in which she stated that a conflict might be created by SEC regulators "walking out the door and going to a firm and leaving everybody to wonder whether they showed some favor to that firm during their time at the SEC." The revolving door has also been blamed for a series of high-profile regulatory failures ranging from the SEC's failures to prevent the Ponzi schemes of Bernard Madoff and R. Allen Stanford to federal regulators' failures to prevent the BP oil spill in the Gulf of Mexico.[27]

The revolving door phenomenon is not new and has, for quite a few years, been on the agenda not only of specific jurisdictions, but also of international organizations such as the Organisation for Economic Co-Operation and Development.[28] It also goes hand in hand with other problems that are liable to undermine the regulator's performance and adversely affect public trust.

First, as mentioned above, the revolving door might help the industry capture the regulator, because she may go job hunting at the regulated firms while still in office. Most scholars believe that the best way to control this is to stipulate cooling-off periods by law. This attitude is mirrored in most jurisdictions by mandatory cooling-off

27. Wentong Zheng, *The Revolving Door*, 90 NOTRE DAME L. REV. 1265, 1268 (2015).

28. ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT, POST-PUBLIC EMPLOYMENT: GOOD PRACTICES FOR PREVENTING CONFLICT OF INTEREST 11-14 (2010) ("OECD Report"); CHRISTOPH DEMKE ET AL., REGULATING CONFLICTS OF INTEREST FOR HOLDERS OF PUBLIC OFFICE IN THE EUROPEAN UNION - A COMPARATIVE STUDY OF THE RULES AND STANDARDS OF PROFESSIONAL ETHICS FOR THE HOLDERS OF PUBLIC OFFICE IN THE EU-27 AND EU INSTITUTIONS (European Commission, October 2007).

period for regulators entering the private sector.[29]

Secondly, the "revolving door" increases the risk that the regulator would later join a lobbying agency hired by the regulated firms in order to promote their interests. This is a slight variation on the first risk described above. Here, the concern is not that the regulator would be more lenient while in office, but that as a lobbyist, she would take advantage of the personal connections she made while in office. Such connections could significantly assist private firms to influence the new regulator to favor their interests over those of the public. A regulator who becomes a lobbyist could use her connections to gain access to confidential information and obtain meetings that otherwise would not take place. In this manner she could slant regulatory decisions in favor of her new clients.[30] The same problems arise in the context of a regulator that now works for a firm that she previously supervised: she might manipulate her personal relationships with her former employees to obtain concessions and special treatment for her new employer. The cooling-off period is also meant to limit the regulator's ability to abuse the connections she has made while in office to advance the goals of the lobbying agency for which she now works..

Thirdly, there is the "side swapping" problem. Sometimes, a regulator handles a statutory process over many months, but does not complete the process before she steps down. If, at the end of her term in office, the regulator starts working for one of the firms that stands to be impacted by that legislation, she might be required to represent this firm in procedures pertaining to the legislation she had handled while still in office. This affords her with exceptional insight as to the shortcomings of the legislation, which she might use in order to thwart the process or cause the proposed bill to be amended according to the interests of the private enterprise for which she is now working. In addition, the former regulator might use inside information. Exposure to sensitive information in her capacity as a regulator might cause a conflict of interest once she starts working for a firm that she used to regulate. [31] Finally, there is also a risk if the former regulator is retained

29. See for example the one-year cooling-off period required under federal law (12 U.S.C. § 1820(k)) for receiving any compensation – as an employee, officer, director, or consultant – from a previously supervised institution. *See also* 18 U.S.C. § 207; *see* 18 U.S.C. §§ 201 *et seq.*; 5 C.F.R §§ 2637 (2004) ("Regulations concerning post employment conflict of interest"), 2641 (2004) ("Post-employment conflict of interest restrictions"); 48 C.F.R. § 3.104-2(b)(3) (2004).

30. OECD report, *supra* note 28, at 27.

31. Many countries are sensitive to this issue and forbid using insider information received while under office. The Canadian law for example forbids providing "advice to his or her client, business associate or employer using information that was obtained in his or her capacity as a public office holder and is not available to the public" Conflict of Interest Act, S.C. 2006, C.9, S.2, art. 34(2) (Can.). Norway

by the regulatory body as a consultant. This practice might cause a conflict of interest if the new regulator favors his predecessor over other advisors because of their personal acquaintance.Among other [32] things, this could also impair public trust of the regulatory body.

Many scholars from different countries have considered the problems arising from the revolving door phenomenon and proposed various solutions. [33] Following this academic debate, several jurisdictions passed laws enforcing cooling-off periods for regulators and other high officials. Many of them stipulate a cooling-off period (normally one to two years) for moving from a regulatory body into the industry, [34] while others, including the U.S., stipulate a cooling-off period in the other direction as well, such that for several months or years, the regulator may not have any communication with the private enterprise for which he used to work, and may not handle any matter directly relating to that enterprise.[35]

Many countries, including Belgium, [36] Australia, [37] Canada, [38] Finland, [39] Ireland, [40] Mexico, [41] Norway, [42] Poland, [43] Turkey[44], the

also published restrictions meant to protect sensitive governmental information, information pertaining to competitors and to strengthen the public's trust in the regulatory institutions (Norway, "Post-Employment Guidelines for the Public Service", (July 2005a); Norway, "Post-Employment Guidelines for Politicians", (November 2005b)).

32. OECD report, *supra* note 28, at 30.

33. *See* Hardy, *supra* note 25. For a leading narrative of the financial crisis of 2007 – 2009 associates the revolving door to conflicts of interest that contributed to distorted credit ratings and to lack of regulation see Elisabeth Kempf, *The Job Rating Game: The Effects of Revolving Doors on Analyst Incentives*, J. FIN. ECON. (forthcoming 2017).

34. OECD report, *supra* note 28.

35. See Exec. Order No. 13490, supra note 6, at § 2.

36. Deontologische code van de Vlaamse volksvertegenwoordigers inzake dienstverlening aan de bevolking [Ethics Code for Members of the Flemish Parliament Concerning Service Provision) of Mar. 17, 1999, http://docs.vlaamsparlement.be/docs/stukken/1998-1999/g7a-1.pdf.

37. *Lobbying Code of Conduct 2008, Statement of Ministerial Standards 2013*, art. 2.24 (Austl.) (available at: www.pmc.gov.au/guidelines/index.cfm.).

38. Federal Accountability Act, S.C. 2006, c. 9 (Can.); Lobbying Act R.S.C. 1985, c. 44 (Can.); Conflict of Interest Act, S.C. 2006, c. 9, S. 2 (Can.); Canadian Government Standards of Ministerial Ethics (2007).

39. Finnish Ministry of Finance, Guidelines for the Transfer of an Official to the Service of Another Employer (2007).

40. Ethics in Public Office Act. 1995(Act No. 22/1995) (Ir.); Standards in Public Office Act 2001 (Act No. 32/2001) (Ir.).

41. Ley Federal de Responsabilidades Administrativas de los Servidores Públicos [LFRA][(Federal Law of Administrative Liabilities of Public Officials], Diario Oficial de la Federación [DO], 13 de Marzo de 2002 (Mex.).

42. *See supra* note 19.

43. Limitations on Conducting Business Activity by Persons Performing Public Functions Act, No. 106, Item 679 (1997) (Pol.).

44. Law on Prohibitions of Post-public Employment, No. 2531 (1981) (Turk.).

EU[45] and the US,[46] have imposed a cooling-off period for transitioning from the public to the private sector. These instructions and regulations impose restrictions on hiring senior public officials and stipulate standards that the regulators must follow while in office. [47] Other countries tried to fend off the problem of "switching sides" by extending the term in public office and increasing the regulators' salaries to try and stop them from crossing the line into the private sector. It is also important to note that some of the most recent debates in the media and in professional literature do not even address the question of whether a cooling-off period is needed. They take it for granted that the answer to this question is an obvious yes and instead focus on the optimal length of this period.[48]

Let us now tackle one of the key questions contemplated by this Article: does the transition of financial regulators from their public office to jobs in the private sector necessarily undermine the public interest, or could such transition, in certain cases, serve the aggregated public utility by improving compliance within the regulated firm? One of the arguments in this paper is that while in office, the regulator undergoes socialization processes. These processes, combined with behavioral biases, will make her a better watchdog within the regulated firm. This has a direct effect on the firm and will increase regulatory compliance. The next two Sections describe these socialization processes, the acquired social identity, and the social biases that will serve as discussion tools in the following Sections of this Article.

V. SOCIALIZATION PROCESSES: SOCIAL IDENTITY

The Social Identity Theory provides that an individual's self-perception also comprises her social belonging and that this, in turn, forms the individual's social identity.[49] A "social identity" is defined as an integral part of the individual's self-perception, arising from the individual's knowledge that she belongs to certain social groups. This knowledge, combined with the emotional value that the individual has attached to her belonging to these groups, creates her de facto social

45. Code of Conduct for Commissioners, SEC (2004) 1487/2 of 24 November 2004 (EC).

46. 12 U.S.C. § 1820(k); 18 U.S.C. § 207; *see* 18 U.S.C. §§ 201 et seq.; 5 C.F.R §§ 2637, 2641 (2004) ("Regulations concerning post-employment conflict of interest"; "Post-employment conflict of interest restrictions"); 48 C.F.R. § 3.104-2(b)(3) (2004).

47. OECD report, *supra* note 28, at 41-92.

48. For a recent example *see* Mervyn King, *The Case for Tough Rules on 'Revolving Door' Jobs: Any Perception of a Conflict of Interest at Central Banks is Damaging*, FIN. TIMES, Aug. 1, 2016.

49. Henri Tajfel, *Social-Psychology of Inter-Group Relations*, 33 ANN. REV. PSYCH. 1, 1-39 (1982).

identity. [50] In other words, an individual's identity comprises, in addition to all the other qualities that turn her into who she is, her social identity. This identity makes the individual feel that she belongs to a group and, in certain situations, to define herself as a "we" rather than as an "I." When this happens, it shows that the individual has psychologically merged with the group. [51]

A social identity gives the individual a sense of belonging and helps him determine who he is, who the "others" are, and how and to which groups he should associate such "others" (a perception of "us" versus "them").[52] Such group affiliations grant the individual utilities arising from the social status of his group, his affiliation with the persons who represent the "ideal" of the group, and the consistency between his behavior and the expectations of the group.[53] Studies of social identity and socialization focus on a person's identity as such that it also refers to his social affiliation or, in other words, his reference group. Other studies have shown that the more connected a person feels to his reference group, the more he changes his behavior and perception of reality to fit the values of the group. [54]

A person can simultaneously belong to several reference groups, but the way she thinks and behaves in the world is influenced by the reference group that wields the strongest influence in that context. [55] As to which of the reference groups has the greatest influence given the context depends on how that person "categorizes" herself in that context. "Self-categorization" occurs when a person knows the "prototype" generated by the social categorization and does whatever she can to be like that prototype. This way, the person loses her self-identity and assimilates with her social group. [56]

In the context of a workplace, the identification levels vary between

50. Henri Tajfel, *Social Categorization, Social Identity and Social Comparison*, *in* HENRY TAJFEL, DIFFERENTIATION BETWEEN SOCIAL GROUPS 61, 61-76 (1978).

51. Jane E. Dutton et al., *Organizational Images and Member Identification*, 39 ADMIN. SCI. Q. 239, 239-63 (1994); Daan Van Knippenberg & Ed Sleebos, *Organizational Identification versus Organizational Commitment: Self-Definition, Social Exchange, and Job Attitudes*, 27 J. ORG. BEHAVIOR 571 (2006); Dennis Veltrop & Jakob de Haan, *I Just Cannot Get You Out of My Head: Regulatory Capture of Financial Sector Supervisors*, 8 (DNB Working Paper No. 410,2014).

52. Blake E. Ashforth et al., *Identification in Organizations: An examination of Four Fundamental Questions*, 34 J. MGM. 325, 372 (2008).

53. George A. Akerlof & Rachel E. Kranton, *Economics and Identity*, 115 Q. J. ECON. 715 (2000).

54. Stuart Albert et al., *Organizational Identity and Identification: Charting New Waters and Building New Bridges*, 25 ACAD. MGM. REV. 13 (2000); Naomi Ellemers et al., *Motivating Individuals and Groups at Work: A Social Identity Perspective on Leadership and Group Performance*, 29 ACAD. MGM. REV. 459 (2004).

55. Ashforth et al., *supra* note 52.

56. Michael A. Hogg & Deborah J. Terry, *Social Identity and Self-Categorization Processes in Organizational Contexts*, 25 ACAD. MGM. REV. 121, 121 – 40 (2000).

employees. The higher the level of identification, the more the qualities that the person attributes to the workplace will merge with the qualities he attributes to himself. When a person completely identifies with his workplace, this is dubbed "organizational identification."[57] It was also found that the more an employee perceives his workplace as socially beneficial or ethical, the faster this identification process occurs, because he will tend to "bask in the reflected glory" of the values that society attributes to his workplace.[58]

The organizational culture of all workplaces is comprised of many things: rules of thumb; an internal language shared by the employees, or jargon; an organizational ideology that helps direct the behavior of individuals within the organization; common standards by which it is decided what is relevant to work and what is not; prejudices; behavioral models; customs; rituals regarding treating colleagues, subordinates, supervisors, and outsiders; and— not the least of which– a common sense that instructs employees on what is considered acceptable and smart behavior in that organization.[59] These organizational behaviors are so ingrained within an organization's culture that, once an employee has learned them, she perceives it as the "natural" way to address the world and problems in the world.[60]

An organizational culture is created and maintained when the individuals joining an organization undergo a socialization process, at the end of which they adapt themselves to the organization. This is a long process because individuals joining an organization sometimes bring norms that are foreign to the organization. They question the organizational culture and the way things are done and try to change them. More experienced employees will teach the new ones to see the world in the same way as the other employees do, and this can take time.[61] In other words, the new employee needs to undergo organizational socialization to acquire the knowledge pertaining to the organizational behavior that he is expected to follow when performing his job.

The result of organizational socialization is that the individual learns which cases to prioritize, how to address daily tasks, how others in the workplace perceive her behavior, etc. Employees who have been working somewhere long enough develop a sort of "common sense," affected by the cultural values of the organization, which they follow

57. Dutton et al., *supra* note 51 at 239-40.

58. *Id.* at 240.

59. John Van Maanen & Edgar H. Schein, *Toward a Theory of Organizational Socialization*, 1-2 (MIT Sloan Sch. of Mgmt., Working Paper No. 960, 1977).

60. *Id.* at 2.

61. *Id.* at 2-3.

in order to solve problems that arise in the course of their workday. This is a perspective that helps them analyze their experience within a certain work task, which also influences their decision-making process.[62] Once an employee has developed this perspective and completed the organizational socialization process, she has, by definition, also formed a "common knowledge" of how things must be handled and how to behave. [63] When an employee changes jobs within an organization or gets a new job with another employer, she needs to adjust to her new setting and is expected to adopt the norms of the new workplace. These transitions can be a shock for the employee, and normally involve mental pressure and confusion. Therefore, it usually takes a relatively long time before the employee internalizes the norms of the new job or organization. The greater the difference between the two jobs, the longer the time it takes. [64]

Socialization processes influence the way we behave in the world, our relationships with other people, and the choices we make. They are of particular relevance to the revolving door phenomenon because they could shed a light on the behavior of financial regulators and possibly even change the discourse surrounding the analysis of adverse effects versus benefits.

VI. BEHAVIORAL BIASES: AVAILABILITY AND LOCK-IN

Before analyzing the advantages and disadvantages of revolving doors in the financial markets, it is necessary to take into account another thing all human beings share: behavioral biases. These biases may change the decision making of an individual joining a new organization and should, therefore, be taken into account when analyzing the revolving door phenomenon. This Section will review the behavioral biases and psychological processes that could come into play in the decision-making process of a former regulator now leading a private sector enterprise or a former leader of a private firm now serving as a regulator: the Availability Bias and the behavioral Lock-in Bias.

The Availability Bias contends that in certain situations, people evaluate the probability of a specific result based on how easy it is for them to recall past events in the same context. For example, people tend to estimate the probability of heart attacks in the middle-aged population based on the number of heart attacks that happened to middle-aged people whom they know. Similarly, people tend to

62. *Id.*at 4.

63. *Id.*

64. *Id.* at 8-10.

estimate the probability of success or failure of a certain kind of business based on the number of success or failure cases of businesses in that category of which they know.[65]

Availability is a useful tool for estimating probability or recurrence, because recurring events "burn" into our available memory more than unusual events. However, the availability bias is affected by other factors in addition to probability or recurrence. [66] One such factor is the way that we are exposed to an event. For example, if someone personally sees a house on fire, they will think that fires are much more common than if they had only read about them in the newspapers. [67] Because of the characteristics of this bias, it is particularly relevant to the debate included later in this Article regarding the transitions of regulators to leading positions in firms that they had previously regulated, and vice versa.

People tend to stick to their old habits. This is known as "Behavioral Lock-In," and occurs mainly when a person has invested time and money toward learning a certain practice, using a product in a certain way, or acquiring a habitual approach to solving problems. In these cases, people follow their old habits even if more effective alternatives could be found. This could be due to organizational learning, personal habits, or cultural bias. [68] In other words, it is almost impossible to teach old dogs new tricks.

It was also found that in the context of working environments, the organization has extensive influence over the employees' habits. Quite often, the way things are done at an organization teaches employees to work in a certain way and fixes their working habits.[69] Once certain organizational behavior has fixed bad habits, the organizational status quo deters any other behaviors that conflict with good habits. An attempt to change employee habits could require much effort and meet active resistance from employees. [70] In other words, once a person is accustomed to doing something in a certain way, she will continue doing it that way, regardless of whether the circumstances have changed.

65. Amos Tversky & Daniel Kahneman, *Judgment Under Uncertainty: Heuristics and Biases*, 185 SCI. 1124, 1127 (1974)

66. Thus, when presented with lists containing names of both men and women and being asked to assess which sex is more common on the list, the answer was affected by the names of famous people – if there were more famous men on the list the subjects thought that there were more men than women on the list and vice versa. *Id.*

67. *Id.*

68. William Barnes et al., *Old Habits Die Hard: Path Dependency and Behavioral Lock-in*, 38 J. ECON. ISSUES 371, 372 (2004).

69. *Id.* at 373.

70. *Id.*

The habits and availability bias literature holds relevant in the context of financial regulators and the quality of regulation as well. Understanding and discussing these psychological processes could alter the way in which we view revolving doors in the capital market.

VII. EITHER SIDE OF THE DOOR: ADVANTAGES AND DISADVANTAGES OF REVOLVING DOORS BETWEEN THE PUBLIC AND PRIVATE SECTOR

As mentioned above, the literature discusses the possible adverse effect of revolving doors on regulators' performance and suggests that this phenomenon increases regulatory capture. However, the direction of the revolving door should also be taken into account, as it likely influences regulatory capture.

A. Advantages of revolving doors – public to private sector

Previously, this Article reviewed the common belief that the revolving door phenomenon should be reduced or eliminated. However, many other considerations show that this phenomenon could, in fact, be positive, especially with regard to the transition of senior officials from the public sector to the private sector. Cooling-off periods are intended mainly to reduce the conflict of interests associated with revolving doors, but they can also cause serious and sometimes unforeseeable damages. [71] Studies have shown that cooling-off periods are liable to limit beneficial interaction between the market and the regulator and even cause the regulator to invest less in acquiring knowledge about the industry that she is to regulate. [72]

These damages were measured empirically by Law & Long, who found that in states in the U.S. that enacted cooling-off periods for regulators, the expertise of the regulators was lower, the regulators spent less time at the office, and invested less in acquiring industry-related knowledge as compared to their colleagues in states without

71. Marc T. Law & Cheryl X. Long, *Revolving Door Laws and State Public Utility Commissioners*, 5 REGUL. & GOV'T 405 (2011). It can be assumed that there will be cases in which the damage is going to be so high that it will eliminate the upside of the cooling-off period. From an economic perspective, the law should restrict regulators from switching sides and working in the regulated industry only if the benefits of such restrictions outweigh its costs. The efficiency criteria which should be used in making such a policy decision is the Kaldor Hicks efficiency criteria which emphasizes the will to maximize the total public welfare. This point is connected also to the Coase Theorem which teaches us of the importance of allocating legal rights efficiently due to the presence of transaction costs which prevent trading in the norm. Ronald H. Coase, *The Problem of Social Cost*, 3 J. L. & ECON. 1 (1960)).

72. Yeon-Koo Che, *Revolving Doors and the Optimal Tolerance for Agency Collusion*, 26 RAND J. ECON. 378 (1995); David Salant, *Behind the Revolving Door: A New View of Public Utility Regulation*, 26 RAND J. ECON. 362 (1995).

statutory cooling-off periods.[73] In other words, an ex-post reduction or neutralizing of the revolving door phenomenon caused an ex-ante decline in the quality of regulation. In another study, several scholars analyzed the career paths of various lawyers who had left the Securities and Exchange Commission ("SEC"). They found that the tougher the lawyers were and the more aggressive the regulations they promoted, the better their chances were of joining a leading law firm after their term with the SEC.[74] These findings are in line with the "regulatory schooling" view, which claims that regulators have an incentive to prefer complex and strict regulation to enhance their future salaries if they choose to switch sides and work for the industry later on.[75] The findings are also in line with the human capital theory, which claims that regulators are hired by the industry according to their expertise and, thus, have a greater incentive to signal their expertise to the industry during their term with the regulatory institution.[76]

If, where revolving doors are allowed, regulators who were not afraid to pass laws against the industry are indeed more sought after at the end of their term than their colleagues who handled the industry with kid gloves, this is an incentive for employees of regulatory agencies to be vigorous and brave enough to regulate even where regulation adversely affects the industry, but upholds the public interest. This would not be possible if the revolving door phenomenon is drastically reduced. Hence, the revolving door between the regulators and the regulated industry seriously motivates regulatory employees to enrich their knowledge and do a good job in order to be more attractive for potential employers in the private sector after their term in public office. Furthermore, the revolving door phenomenon has another positive aspect: it enables the public sector to recruit better experts and to pay a salary which is relatively low compared to the private sector. This is because excellent experts are willing to contribute a few years of their lives in order to get to know the public sector from the inside, knowing that this knowledge will be sought

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73. Law & Long, *supra* note 71.

74. Ed DeHaan et al.,, *Does the Revolving Door Affect the SEC's Enforcement Outcomes?*, J. ACCT. & ECON. (forthcoming), *available at* https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2125560.

75. David Lucca et al.,, *The Revolving Door and Worker Flows in Banking Regulation*, 65 J. MONETARY ECON. 17, 18 (2014); Sumit Agarwal et al., *Inconsistent Regulators: Evidence from Banking*, 129 Q. J. ECON. 889, 889 – 938 (2014). Of course, this is not to say that more complex regulation is also more strict, however, if we combine these claims with the findings of Law & Long we can assume that at least some of that regulation is also stricter. Law & Long, *supra* note 71.

76. Heski Bar-Isaac & Joel Shapiro, *Credit Ratings Accuracy and Analyst Incentives*, 101 AM. ECON. REV. 120, 120 (2011).

after by the private sector later on.[77] Not only that, but also one benign view of lobbying is about information transmission of various groups making their case.[78] This can be facilitated by a revolving door, as it means the two parties "speak" the same language, which can allow for better regulatory outcomes. Consequently, the more we curtail the revolving door phenomenon, the more we reduce the quality of regulation.[79] These studies show that regulations intended to prevent revolving doors adversely affect the motivation of employees in financial regulatory institutions to improve their knowledge and skills.

In addition, there is another cost to the quality of supervision by restricting or prohibiting the revolving door phenomenon. When a regulator switches sides and starts working as an executive in one of the firms which she previously regulated, she brings with her a different attitude to rules and regulations. This attitude includes her understanding of the importance of regulation and of its goals, as well as the habits which she developed during her term as a regulator, especially with regard to decision-making and problem-solving.[80] As a result of the behavioral biases and the socialization processes discussed in preceding Sections, someone who has served as a regulator and understands the rationale behind regulation and the need for compliance will be more likely to enforce strict procedures inside the firm with regard to compliance as opposed to someone who came to the job from the private sector.

Based on the Availability Bias, a regulator who crosses the line to the private sector will continue to evaluate situations she encounters in the private market through her situational stances as a regulator. The ex-regulator was likely exposed to cases in which lack of compliance led to regulatory sanctions or the destabilization of a financial firm. According to the Availability Bias, people evaluate the occurrence of certain results based on their recollection of the past—especially if they were directly exposed to it.[81] As such, it is likely that the ex-regulator will be more cautious and will comply more with the regulations compared with executives who never served in regulatory positions. Furthermore, the habits which the ex-regulator accumulated during her term as a regulator follow her to the new position in the

77. DeHaan et al., *supra* note 74.

78. Adam William Chalmers, *Trading Information for Access: Informational Lobbying Strategies and Interest Group Access to the European Union*, 20 J. EURO. PUB. POL'Y 39, 40 (2013).

79. Toni Makkai & John Braithwaite, *In and Out of the Revolving Door: Making Sense of Regulatory Capture*, 12 J. PUB. POL'Y 61, 72-73 (1992).

80. Once one has served in a regulatory position and has moved to an executive position in one of the regulated firms, there may be a better understanding of the exact reasons for the regulation and supervision. Outward people movement then may especially be useful in complex areas.

81. Tversky & Kahneman, *supra* note 65, at 1127.

private sector. If someone is accustomed to solving problems as a regulator would, she will continue to approach similar problems in a like manner in her new private sector position. Even if the external conditions change, such as a change in the workplace, once a person is accommodated to doing things in a certain manner, she will continue to do them the same way.[82]

The literature on socialization processes and on social identity strengthens this reasoning.[83] According to the social identity theory described earlier in this Article, part of our identity of the "self" is derived from belonging to a group. In turn, this affects the individual's social identity.[84] In the context of a financial regulator who passes through the revolving door and starts working for the regulated industry, as her social group remains at the regulatory institution for which she used to work , she will be more careful to avoid decisions that will cause her social group in the financial regulatory institution to question her motives or personality (according to the Social Identity Theory).[85] Regulators acquire reputations and connections while learning how to adapt to the social norms inside the regulatory institution. The findings of the literature dealing with socialization processes in an office setting point out that when an employee changes her position and transfers to a different job or position, it takes time until her social group changes. Thus, it can be assumed that the day after the regulator stops being a regulator she will continue to adhere to the same norms and relate to the employees in the regulatory institution for which she used to work as her colleagues. What these colleagues think of her will still matter. It is very unlikely that a former regulator will abandon her social relationships and worldview, and free herself of the organizational culture and social identification relating to her former workplace, only because she has changed her career.[86]

Therefore, cooling-off periods, which are meant to distance the regulator from her social group inside the regulatory institution, make her less attractive to the regulated industry, and less vulnerable to capture during her term as a regulator, might cause more harm than

82. Barnes et al., *supra* note 68, at 373.

83. Alexander S. Haslam et al.,, *Sticking to our Guns: Social Identity as a Basis for the Maintenance of Commitment to Faltering Organizational Projects*, 27 J. ORG. BEHAV. 607 (2006); Ashforth et al., *supra* note 52; Tajfel, *supra* note 49.

84. Tajfel, *supra* note 49.

85. This claim is strengthened by the research on social identity which shows that it takes a long time for an employee to change her social group from one group to the other. Maanen & Schein, *supra* note 59, at 8–10.

86. *Id.* See also the empirical work of DeHaan et al., *supra* note 74, at 11, who claim something similar with regards to the other side of the revolving door: they claim that the longer a regulator has served in the private sector the more he tends to identify himself with it.

good. This is because they also cool off the identification of the regulator with her social group within the regulatory institution and her behavioral biases, as work habits tend to wear off after a while and the availability of events is strongest when those events were recent. On the other hand, it seems that the threats of the revolving door come from the other side–when people enter the regulatory institution after serving in the private sector for a while—especially inside the regulated firms.

B. disadvantages of revolving doors – private to public sector

The revolving door phenomenon has two sides and also includes employees who enter the regulatory institutions after being employed by the regulated firms.[87] This side of the revolving door has many advantages, such as enriching the regulatory institution with knowledge of employees who worked for the industry. These former employees understand the material and know exactly how things work in the regulated firms. This knowledge also includes also an institutional and business understanding of the regulated industry, as well as practical knowledge with regards to how things are done. This type of knowledge might positively contribute to the regulatory institution and to the understanding of the optimal regulatory solutions to perceived market failures. However, transferring from the regulated industry into the regulatory institution could also result in the regulator being unknowingly captured. In fact, there is some empirical evidence that the appointment of a former regulated firm employee to an executive position within the regulatory institution does increase the likelihood of regulatory decisions that favor the industry.[88] But why does this happen? In this context, the self-categorization of the individual is highly important.[89] Self-categorization affects the individual's self-determination: when an individual categorizes herself into a group, her own personal identity is somewhat merged with the group. Regulators who are involved with the industry identify with it from a psychological point of view. This might cause them to provide the regulated industry with benefits or regulate it less strictly. In other

87. A few examples were mentioned in Eric Ben-Artzi's opinion article: "Robert Rice, the chief lawyer in charge of the internal investigation at Deutsche in 2011, became the SEC's chief counsel in 2013. Robert Khuzami, Deutsche's top lawyer in North America, became head of the SEC's enforcement division after the financial crisis…" Eric Ben-Artzi, *We Must Protect Shareholders from Executive Wrongdoing*, FIN. TIMES, Aug. 18, 2016.

88. William T. Gormley, *A Test of the Revolving Door Hypothesis at the FCC*, 23 AM. J. POL. SCI. 665, 681 (1979); Stavros Gadinis, *The SEC and the Financial Industry: Evidence from Enforcement Against Broker-Dealers*, 67 BUS. L. 679, 725–26 (2012).

89. DeHaan et al., *supra* note 74, at 8–9.

words, "Social identification with the financial sector would lead financial supervisors to internalize group-defining (i.e. financial sector) characteristics in their self-concept and strive for behaviors that are prototypical for this sector…"[90]

Such identification with the regulated industry might cause the new regulator to implement norms and set a regulatory standard that favors the regulated firms and is against the public interest. In such circumstances, the regulator is no longer objective. When a regulator is not objective and favors the interests of the regulated industry, she is actually captured by the industry without being aware of it.[91]

It is reasonable to assume that an individual who has worked for years in a regulated firm and with the employees in the regulated industry will still maintain good and close connections to her former colleagues. These close connections might cause the regulator, sometimes unknowingly, to soften the regulatory requirements in order to assist the regulated industry.[92] Indeed, empirical research in this area proves that the longer the regulator worked in the private sector, the greater the risk of capture.[93] Here, the fear is that the regulator will not feel comfortable burdening her former colleagues and supervisors and will act to please them.

In addition, a regulator who transfers from the regulated industry to the regulatory institution might be caught in a mindset of promoting business at all cost. In fact, such a regulator is likely to view the issues at hand with an industry eye and sympathize with the regulated industry.[94] This too might interfere with the ability to regulate according to what is needed in order to promote the public interests. This claim is further strengthened when the behavioral biases

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90. Veltrop & De Haan, *supra* note 51.

91. *Id.*

92. DeHaan et al., *supra* note 74; Maanen & Schein, *supra* note 59, at 8–10.

93. DeHaan et al., *supra* note 74, at 8–9; Kevin L. Young et al., *Beyond the Revolving Door: Advocacy Behavior and Social Distance to Financial Regulators*, 19 BUS. & POL. 327, 327 (2017) (Finding that: "The financial system is governed not just by formal rules but also by social relationships that pervade the elite strata of society. Understanding such dynamics entails understanding complex relational ties between actors, a task that can be facilitated through the use of network analysis. We argue that a latent feature of interest to scholars of the political economy of finance is one of social distance, which is a measurable concept. Using new data from the financial sector, we measure the social distance between a range of financial firms and one key regulator, the U.S. Securities and Exchange Commission (SEC), over time to assess whether or not social distance is related to organizations' advocacy behavior. We find a positive relationship between how close a given organization is to the SEC and how often it engages in advocacy. The result persists when we control for numerous factors related to organizational characteristics, firm size, and when we measure advocacy frequency in different ways.").

94. Per J. Agrell & Axel Gautier, *Rethinking Regulatory Capture*, *in* RECENT ADVANCES IN THE ANALYSIS OF COMPETITION POLICY AND REGULATION286, 291 (Joseph E. Harrington & Yannis Katsoulacos eds., 2012).

discussed previously are taken into account.[95] If we consider the Availability Bias, it is very likely that the approach of a regulator coming from the regulated industry will be more lenient in supervising the industry than that of someone whose career was established inside the public sector. This is because the individual probably encountered cases while working for the industry in which the regulator disrupted her work and interfered with her ability to maximize profits for the shareholders of her firm. In addition, behavioral lock-in is also expected to occur on this side of the revolving door. An employee coming to the regulatory institution from the regulated industry will bring with her the old habits she acquired in her previous job in the market. These habits might (and indeed very likely will) include an approach which views regulation as an obstacle. Therefore, the regulator may attempt to reduce the regulatory burden. This might cause the regulator to be more cautious when regulating the industry, sometimes even to the point where regulatory powers are overly restrained and the public welfare, which the regulator is supposed to promote, is damaged. This understanding is reflected in several laws and regulations around the world which also require cooling-off periods when entering the public sector. For example, upon the inauguration of Barack Obama, the White House issued a set of rules that try to decrease the negative influence of revolving doors when entering the public sector. It did so by setting a two-year cooling-off period under which all individuals entering the public sector are not allowed to work on anything related to their previous positions in the private sector.[96] Indeed, such an approach seems sensible when dealing with this private-to-public side of the revolving door and is generally recommended for all jurisdictions.

VIII. SUMMARY AND CONCLUSIONS

Revolving doors in the financial market are a prevalent phenomenon and have been broadly discussed in the literature and in the press. In an attempt to mitigate the negative impacts of this phenomenon, many jurisdictions have enacted cooling-off periods for individuals who choose to switch from working as regulators to working for the regulated industry. The idea behind cooling-off periods is that, without them, it will be easier for the regulated industry to capture their regulators.

This Article, however, questions the benefits of cooling-off periods

95. Barnes et al., *supra* note 68, at 372.

96. Exec. Order No. 13490, *supra* note 6, sec. 2.

when individuals move from the public to the private sector. It claims that an individual who served in a regulatory position and starts working for the regulated industry brings with her to the job an understanding of the importance of regulation and the knowledge of how to implement it. This, combined with her habits, her availability bias, social connections, affiliations to the employees working inside the regulatory institution, and with the socialization processes she underwent while still inside the regulatory institution, will lead her to be a much more cautious manager with regard to adhering to regulatory demands. Cooling-off periods in this context might actually cause more harm than good, as they will detach the former regulator from her social group in the regulatory institution and have a cooling effect on her behavioral biases which work in favor of the public's welfare.

The problem, according to this Article, lies on the other side of the revolving door—when an employee enters the regulatory institution after working for the regulated industry. It is here that the behavioral biases and socialization processes which the individual underwent during her time at the regulated industry work against the public interest and might interfere with her ability to regulate the industry diligently. Therefore, cooling-off periods are needed on this side of the revolving door in order to ensure that the newly appointed regulator is free of the influence of the industry and is not captured by it.