The Invisible Hand of Law: Private Regulation and the Rule of Law

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Introduction

The early 1980s—when "politics and ideology . . . turned arse-over-tit," as E.P. Thompson once described it—was, in the less colorful language of David Harvey, a "revolutionary turning point in the world's social and economic history."[1] Law was not immune to the sweeping changes taking place.[2] Until the 1980s, and over the previous half century, law had served

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(albeit unevenly and incompletely) as the main institutional vehicle for policing corporations in aid of public interests, thereby protecting people, communities, and the environment from corporate excess and malfeasance.[3] Over the course of the 1980s and thereafter, however, law's protective role began to diminish, and privately promulgated voluntary regimes (hereinafter "private regulation"[4]) emerged in its place.[5]

Importantly, no such diminishment occurred in relation to law's parallel and prominent role in protecting corporations and their interests. Here, state legal regimes continued to operate as robustly as ever; incorporate companies; establish their mandates; protect their rights as "persons"; shield their managers, directors, and shareholders from legal liability; compel their officers to prioritize their "best interests" (typically construed as increasing shareholder value); articulate and enforce their contract and property rights; and repress dissidents and protesters who opposed their growing power. Corporations—indeed, corporate capitalism—could not exist without these legal foundations and supports, which taken together represent a massive infusion of state legal power into society.

Despite that massive infusion, many private regulation advocates and commentators presume that globalization eviscerates state legal power, and prescribe, on that basis, that private regimes should take law's place.[6] This Article challenges that presumption and prescription. Following examination of the rise of private regulation in Part I, Part II reveals how private regulation advocacy and commentary often obscure, and effectively render invisible, law's robust role in constituting and protecting corporations, thereby exaggerating globalization's alleged diminishment of state legal power. Part III claims that private regulation weakens the rule of law and its democratic potential, with the effect, Part IV explains, of exacerbating corporate threats to public interests.

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one among many normative-regulatory regimes, reduce legal decisions to policy choices, and thereby lose sight of the critical point of the exercise." *See id.* (paraphrasing, she notes, Martti Koskenniemi, *The Fate of Public International Law: Between Technique and Politics*, 70 MOD. L. REV. 1 (2007)).

3. *Cf.* Fabrizio Cafaggi & Andrea Renda, *Public and Private Regulation: Mapping the Labyrinth* 1, 1 (Ctr. Eur. Pol'y Stud., Working Paper No. 370, 2012) [hereinafter Cafaggi & Renda, *Labyrinth*].

4. I use the term "private regulation," rather than "transnational private regulation" (a common term in the literature) to connote that self-regulation and other forms of private regulation are advocated and active within states, as well as within international realms. *See* Ronen Shamir, *Socially Responsible Private Regulation: World-Culture or World-Capitalism*?, 45 L. & SOC. REV. 313, 313 (2011) [hereinafter Shamir, *Socially Responsible Private Regulation*].

5. *See* Cafaggi & Renda, *Labyrinth*, *supra* note 3, at 1–2, 7. While private regulation is often referred to in the literature as "soft law," I treat it as a non-legal albeit normative and regulatory practice, following the definition of law stated in note 2. *Cf.* Fabrizio Cafaggi, *New Foundations of Transnational Private Regulation*, 38 J. L. & SOC. 20, 36 (2011) [hereinafter Cafaggi, *New Foundations*].

6. Notably, the literature on private regulation is vast and varied: while some commentators advocate its virtues and prescribe it, others limit their work to describing and analyzing its development, and still others are critical of it. Cafaggi & Renda, *Labyrinth*, *supra* note 3, at 4–5. This paper challenges the first group of scholars, draws upon the second, and is sympathetic to the third.

I. The Rise of Private Regulation

Over the last several decades, a rapidly expanding network of private regulation regimes has emerged to create a new mode of international governance.[7] Taking a variety of forms, these regimes vary in their complexity, the range of organizations they include, and the degree to which they are monitored and enforced.[8] Corporate social responsibility (CSR) and related self-regulation programs rely upon voluntary standards and codes of conduct, promulgated by companies and industry groups, and sometimes monitored by third-party agencies.[9] NGO-led regimes invite outside, albeit private, agencies to set voluntary standards in cooperation with companies and industry groups, and often include monitoring mechanisms and reporting requirements.[10] Expert-led models feature organizations, such as the International Organization for Standardization, which establish norms for different industries and for industry as a whole.[11] Multi-stakeholder models involve collaborations among companies, NGOs, expert groups, industry associations, and governments to set and monitor standards (though, importantly, governments in these regimes serve as partners and supports rather than sovereign or legal regulators, thus eschewing traditional regulator-regulated hierarchies).[12]

While in theory private regulation norms may complement or crystallize into legal norms, in practice the gains of private regulation often come at the expense of public norms, "push[ing] the once-central 'official' or state law to the global edge," as Muir-Watt describes it.[13] "Widespread advocacy for forms of private regulation in lieu of public regulation," according to Caffagi and Renda, has lead "governments [to] award priority

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7. *See* TIM BÜTHE & WALTER MATTLI, THE NEW GLOBAL RULERS: THE PRIVATIZATION OF REGULATION IN THE WORLD ECONOMY 1–2 (2011); Saskia Sassen, *The State and Globalization*, *in* THE EMERGENCE OF PRIVATE AUTHORITY IN GLOBAL GOVERNANCE 91, 91 (Rodney B. Hall & Thomas J. Biersteker eds., 2002); Kenneth W. Abbott & Duncan Snidal, *International Regulation Without International Government: Improving IO Performance Through Orchestration*, 5 REV. INT. ORGAN. 2 (2010); Larry Catá Backer, *Private Actors and Public Governance Beyond the State: The Multinational Corporation, the Financial Stability Board and the Global Governance Order*, IND. J. GLOBAL LEGAL STUD. 751, 751 (2011); Horatia Muir-Watt, *Private International Law Beyond the Schism*, 2 TRANSNAT'L LEGAL THEORY 347, 347 (2011).

8. Abbott & Snidal, *supra* note 7, at 4–9 (for a comprehensive review of these various types of regimes, with numerous examples).

9. *See, e.g.*, *id.* at 7, 38 (describing GAP's individual labor rights scheme of 1992 and the International Council on Mining and Metals sustainable development principles of 2003).

10. *See, e.g.*, *id.* (describing the Rugmark labeling scheme, created in 1994 to control child labor in the carpet industry; the CERES principles on environmental practice and reporting; and Amnesty International's Human Rights guidelines for Companies).

11. *See, e.g.*, Fillipo Fontanelli, *ISO and Codex Standards and International Trade Law: What Gets Said is Not What's Heard*, 60 INT'L & COMP. L.Q. 895, 900 (2011) (discussing various industry standards promulgated by the International Organization for Standardization).

12. *See, e.g.*, Abbott & Snidal, *supra* note 7, at 2, 40 (discussing the 1997 Global Reporting Initiative's standards for social and environmental reporting and the 2004 World Fair Trade Organization's standards for fair trade).

13. Muir-Watt, *supra* note 7, at 352.

ket" is something different than, indeed separate from, "traditional state control"—a presumption similarly implied by most arguments in favor of private regulation.[26] As a consequence of globalization, those arguments hold, MNCs (the "realm of the market") are able to elude state law ("traditional state control") and that, in turn, makes necessary the introduction of non-state, private regulatory measures.[27] When Abbott and Snidal describe "traditional state-based mechanisms" and "mandatory regulation" solely in terms of laws that constrain corporations, but not those that protect and enable them, law's constitutive and enabling role is obscured.[28] When John Ruggie highlights "governance gaps created by globalization—between the scope and impact of economic forces and actors, and the capacity of societies to manage their adverse consequences," those economic forces and actors are, again, implicitly detached from, rather than rooted in, societies' governance and legal structures.[29] When, more generally, neoliberal notions "stress[ ] the importance of markets and open economies for growth and [seek] a more limited role for the state," as Trubek describes them, the role of states in constituting and enabling markets and open economies is implicitly negated.[30]

hedges against public regulation[38]) separate from those of their owners and officers;

- Limit investors' liabilities to the amounts they invest, and thus reduce their exposure to risk, and also enable companies to evade tax and legal liability through subsidiary schemes;[39]
- Create and enforce corporations' contract[40] and property[41] rights (in the form of real, commercial, and intellectual property, as well as shares and other financial instruments);
- Implement new "command and control" policing of anti-corporate protestors—"heavy police presence, . . . increase[d] police powers[, and] surveillance of potential protest organizers, with databases of personalities and activities," as one commentator describes it;[42]
- Constitute and join international trade liberalization regimes that propel the very globalization processes that limit states' capacities to regulate MNCs in aid of public interests;[43]
- Require corporate directors and managers to prioritize the "best interests of the corporation" over all other interests—including social and environmental interests—in all of their decisions and actions.[44]

Making visible these different ways that law constitutes, enables, and protects MNCs disaffirms some key presumptions behind private regulation advocacy. No longer, for example, can globalization plausibly be presumed to diminish states' rule-making authority over MNCs when those MNCs are *dependent* on states' rule-making authority to exist and operate. No longer can a "governance gap" intelligibly be proposed when governance continues robustly, albeit in the service *of* MNCs, rather than in protecting others *from* MNCs. No longer can we imagine "a dearth of (state and non-state) normativities," as Muir-Watt describes it, when "despite and sometimes because of their multiplicity [extant normativities] do not achieve—and indeed may conspire to impede—the tethering of private interests in the name of the global good."[45]

or questioned, when, as is the case in much private regulation discourse, law's constitutive, enabling, and protective role for MNCs is invisible.

III. Private Regulation and the Rule of Law

In *Whigs and Hunters*, historian E.P. Thompson describes a hideous episode in law's long history of enforcing class power.

quishes some economic power he or it possesses in law's absence, and the hierarchy created through wealth is regulated," thereby demonstrating that shared subjection to the sovereignty of law "displaces cruel and brutal realms of private sovereignty, and thereby serves egalitarian ends."[61]

Public regulation can thus be understood as animated and justified by "ideal notions" akin to those Thompson describes, even while its actual record falls notoriously short of those ideals (due in part to relentless industry pressure on governments before, during, and since the time of the New Deal[62]). Indeed, by the early 1980s, the very idea (and ideal) of public regulation as a means for protecting public interests was under attack, and with the ensuing rise of neoliberalism, cynicism and suspicion quickly set in.[63] Today, the inadequacies of public regulatory regimes are legion and notorious—agency capture, revolving doors (between industry and agencies), undue corporate influence through lobbying and electoral campaign financing, pork barreling and earmarking, corruption, underfunded and inadequate enforcement, and, of course, the pressures of globalization—and contribute to a growing chasm between the ideals of public regulation, and the actual operations of public regulatory systems.[64]

As a result, many today—private regulation advocates chief among them—believe public regulation is a lost cause and that its hierarchical, legal, and sovereignty-based control of MNCs should give way to heteroarchical, voluntary, and private norms.[65] New forms of global govern-

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61. ROBIN L. WEST, RE-IMAGINING JUSTICE: PROGRESSIVE INTERPRETATIONS OF FORMAL EQUALITY, RIGHTS, AND THE RULE OF LAW 173, 175 (2003). In a similar vein, West notes "the potential of law . . . to serve as a challenge to the preferences and desires that are otherwise reflected in, and gratified in, various exchange markets, and to do so . . . toward the end . . . of enhancing human wellbeing." *Id.* at 174. Importantly, however, while 'public regulation' connotes mandatory legal regimes (ones composed of rules, principles, and standards promulgated and enforced by sovereign state institutions and recognized as binding within their jurisdictions), that does not limit it to strictly command-and-control regimes. There is a large and live debate about new modes of regulation that maintain a mandatory legal character—thus being neither private nor voluntary—while taking a non-command-and-control form. *See, e.g.*, discussions of "co-regulation" in BAKAN, CHILDHOOD UNDER SIEGE, *supra* note 1, at 60, 64–65, 259; "principle-based regulation" in Paul Latimer and Phillip Maume, PROMOTING INFORMATION IN THE MARKET FOR FINANCIAL SERVICES: FINANCIAL MARKET REGULATION AND INTERNATIONAL STANDARDS 217–234 (2015); and "responsive regulation" in Christine Parker, *Twenty Years of Responsive Regulation: An Appreciation and Appraisal*, 7 REG. AND GOVERNANCE 2 (2013).

62. *See* BAKAN, THE CORPORATION, *supra* note 25 at 86.

63. *See id.* at 21.

64. *See, e.g.*, *id.* at 162.

65. *See generally* Colin Scott et al., *The Conceptual and Constitutional Challenge of Transnational Private Regulation*, 38 J. L. & SOC'Y. 1 (2011). One can challenge this view—as I do—while still acknowledging that 1) states have lost some control over their territories, borders, populations, and institutions (including corporations), especially as international organizations morph into global governors and regulators; 2) technological innovation fuels economic interdependence; 3) major corporations operate in multiple nations; and 3) environmental degradation, migration, human rights, and terrorism defy (and deny) state borders (*see* Jean Cohen, *supra* note 2). These factors may present challenges for mandatory legal regulation, but not reasons to abandon the project in favor of private alternatives.

IV. The Limits of Private Regulation

The rise of CSR neither challenged nor changed the corporation's legal core, which still features the "best interest of the corporation" principle, and its requirement that managers and directors prioritize shareholder value.[81] The constraints imposed by the principle on corporations' pursuit of social and environmental values are indeed accepted by most CSR advocates, who ask companies to find synergies between business interests and other values, but not to sacrifice the former to the latter. "The essential test that should guide CSR is not whether a cause is worthy," as Porter and Kramer state, "but whether it presents an opportunity to create *shared value*—that is, a meaningful benefit for society *that is also valuable to the business*."[82] A corporation's CSR agenda should seek opportunities to "achieve social and economic benefits simultaneously," to "reinforce corporate strategy by advancing social conditions," and to "make the most significant social impact and reap the greatest business benefits."[83]

Contemporary CSR is largely defined and inspired by Porter and Kramers' "shared value" approach,[84] which its advocates distinguish from earlier, narrowly strategic CSR—"hypocritical window dressing," as Milton Friedman once described it.[85] Though the latter may still define much corporate practice,[86] they say, the tide is turning. "Defensive, minimalist responses to social and environmental issues will be replaced by proactive strategies and investment in growing responsibility markets," according to Wayne Visser, who describes the new approach as CSR 2.0.[87] "Reputation-conscious public-relations approaches to CSR will no longer be credible

81. For an exploration of these limits, see *id.*

82. *See* Porter & Kramer, *supra* note 76, at 12 (2006) (emphasis added).

83. *Id.* at 16.

84. See DAVID VOGEL, THE MARKET FOR VIRTUE: THE POTENTIAL AND LIMITS OF CORPORATE SOCIAL RESPONSIBILITY 19–21 (2005) for examples of the business case for CSR ("the

There are good reasons to be skeptical,[93] however, especially when, as already noted, new approaches to CSR demand only that corporations *share* value with social and environmental concerns, but not *sacrifice* it to those concerns. As such, while the new CSR undoubtedly inspires broader social and environmental initiatives from MNCs, its demand that corporations pursue social and environmental good only when it helps them do well—that CSR initiatives necessarily "intersect with [an MNC's] particular business," as Porter and Kramer describe it[94]—profoundly narrows possibilities.

Take, for example, Shell Oil, which recently signed the Trillion Tonne Communique, the self-proclaimed "progressive business voice" on climate change.[95] On first glance, Shell, currently involved in some of the world's most controversial fossil fuel development and exploration, seems a surprising party to the Communique, not least because it is the only major oil company to sign on.[96] Shell—a sixty percent partner in the Athabasca Oil Sands Project,[97] major backer of the Keystone Pipeline,[98] and heavily involved across the globe in hydraulic fracturing ("fracking")[99]—is regularly targeted by protestors,[100] environmental and climate change advo-

communities; *Coke Raises More than $2 Million to Save Polar Bears*, COCA-COLA, http://www.coca-colacompany.com/our-company/coke-raises-over-2-million-to-save-polar-bears (last visited April 25, 2015).

93. The "rhetoric of governments 'partnering' with industry continues to resonate," as Lorne Sossin has observed, though, as he states, there are good reasons to be skepti-

cates,[101] and ambitious regulators.[102] "We're very conscious," states Marvin Odum, president of Shell Oil in the United States, "of the fact the world is likely moving to a place of regulating carbon in some respect."[103]

Joining that movement, rather than opposing it, and working to ensure it yields favorable results for the company, has been key for Shell and helps explain why it signed the Communique. "What's important to us, and what our primary push has been with governments," says Odum, "is ensuring . . . that [regulations are] market-based systems to allow carbon regulation to happen at the lowest possible cost."[104] Cap-and-trade is the preferred approach, he says, "one of the clearest examples of a market-based system."[105] Carbon capture and storage is another option, says Odum, "a great example of efforts to reduce carbon emissions from oil sands."[106] The ultimate goal, says Odum, is to find the "right policy framework—like a price on carbon—that companies could do on their own."[107]

Shell's preference for voluntary market-based regulation is well-served by the Communique which, in line with "shared value" CSR, articulates a "pro-business" position, presumes climate change solutions "can and should be delivered in ways that create new business opportunities, and keep costs manageable," and prescribes "policies that work with the market to incentivize the private sector."[108] These proposed solutions—which explicitly include Odum's preferred approaches of carbon pricing, capture, and storage[109]—should, the Communique states, "lead to economic benefits, while insulating the global economy from risks caused by a planet that warms beyond two degrees."[110]

Shell really has nothing to fear from the Communique and indeed much to gain by supporting it. Not only does the Communique endorse market-driven regulatory solutions, including the very ones Shell advocates, but it also helps "shap[e] the narrative" on business and climate change—as the Communique describes one of its goals[111]—in favor of those solutions, while simultaneously signaling to consumers and governments that the company cares and is doing something about climate

101. *See* Phuong Le *supra* note 100; Anastasia Killian, *Environmental Groups Continue Attempts to Thwart Arctic Oil dd climate*

These examples (and there are many others that might be added) show how CSR, even in its newly broadened ideations, remains limited and problematic: one step forward, perhaps, for its providing some protection of social and environmental values, but three steps back for molding regulatory debates to prioritize business interests, helping justify governments' retreat from mandatory norms, and promoting narratives of corporate change to pacify potential critics.[119] It would, of course, be different if there were broad convergence among business, social, and environmental interests. In reality, however, the social and environmental initiatives that plausibly converge with business interests constitute a "very narrow subset that involve little cost, little risk, and little disruption to business as usual," as Charles Eisenstein describes it.[120] That is the conclusion not only of commentators,[121] but also many CEOs who report feeling caught in cycles of "individual, small-scale projects, programs and business units with an incremental impact on sustainability metrics," while "their responsibilities to more traditional fundamentals of business success, and to the expectations of markets and stakeholders, are preventing greater scale, speed and impact."[122] Sustainability cannot be achieved, these CEOs believe, "without radical, structural change to markets and systems."[123]

The limits of "shared value" CSR, and, by implication, private regulation, are profound, which is likely the reason "no significant move has been made [through private regulation] . . . to tame multinational corporate misconduct in respect of [major global issues]."[124] When social and environ-

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119. Stacey Mitchell similarly describes Walmart's sustainability programs as "one step forward and three steps back" as quoted in Dauvergne & Lister, *supra*, note 112, at 23. Dauvergne & Lister add that "the big brand takeover of sustainability is shifting the purpose and goal of sustainability governance toward the need to create business value." *Id.* at 25.

120. Charles Eisenstein, *Let's Be Honest: Real Sustainability May Not Make Business Sense*, THE GUARDIAN, Sustainable Business Blog (Jan. 8, 2014, 09:33 AM), http://www.theguardian.com/sustainable-business/blog/sustainability-business-sense-profit-purpose.

121. *See, e.g.*, Megan Bowman, *The Limitations of Business Case Logic for Societal Benefit & Implications for Corporate Law: A case study of climate friendly banks* (2014), *presented at* 2014 Conference on Empirical Legal Studies (CELS), Univ. of Cal. at Berkeley, November 6-8, *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2489116; Andrew Hoffman, *Climate Change Strategy: The Business Logic Behind Voluntary Greenhouse Gas Reductions*, 47 CAL. MGMT. REV. 21, 23 (2005); Markus J. Milne, Helen Tregidga and Sara Walton, *Words Not A.02820.041 Tw(R)Tj0.006 0 0 5.8 337.29 242.1kus21,eTβ.50*

mental interests depend for their protection on measures that must cohere with business interests, the "severe hardship, injustice, imbalance and crisis linked to the rise of private global rulers"[125] are likely to go largely unchecked. Even Porter and Kramer acknowledge that "social agendas" do not always align with corporate and industry interests, and that in many instances, "NGOs or government institutions . . . are [thereby] better positioned to address them."[126] Yet they, along with many other CSR and private regulation advocates, continue to promote the notion that corporations—"the most powerful force for addressing the pressing issues we face"[127]—should take the lead on social and environmental issues, while governments retreat to positions as "rule takers" from their traditional roles as "rule makers."[128]

Conclusion

It has been more than thirty years since Dean Paul Carrington chastised critical legal studies scholars for "profess[ing] that legal principle does not matter," calling on them to resign their law school posts.[129] His portrayal of critical legal studies was a caricature and his prescriptions shrill,[130] but his central claim that legality must be defended against nihilism bears repeating as private regulation proponents "profess that legal principle does not matter," or matters less, for constraining MNCs in aid of public interests.[131] "The time is ripe," Galit Sarfaty observes, to reassert the need "for corporate accountability through mandatory regulations," especially as we slide into broad acceptance of non-legal regulation in lieu of law.[132] Though voluntary commitments may help companies "deflect[ ] state regulation and express[ ] their good 'corporate citizenship,'" the "need for binding regulation" remains.[133]

There is also, however, a need to consider the "binding regulations" already in place that serve to constitute corporations, enable their operations, and protect their interests. As Part II reveals, these tend to be downplayed by private regulation advocates and commentators who, as a result, make exaggerated claims about globalization's diminishment of state legal authority.[134] Corporations, as this Article argues, are legal constructs, created only through the operation of state law. They are rooted within and

125. *Id.* at 406.
126. Porter & Kramer, *supra* note 76, at 64.
127. *Id.*
128. *See* Cafaggi & Renda, *Labyrinth*, *supra* note 3, at 21.
129. *See* Paul D. Carrington, *Of Law and the River*, 34 J. LEGAL EDUC. 222, 227 (1994).
130. *See* Gary Minda, *Of Law, the River and Legal Education* 10 NOVA L. REV. 705, 705 (1985–1986); *Nihilism and Academic Freedom: Introduction and Correspondence*, 35 J. OF LEGAL EDUC. 180 (1985).
131. *See* Carrington, *supra* note 129, at 227.
132. *See* Galit A. Sarfaty, *Human Rights Meets Securities Regulation*, 54 VA. J. INT'L L. 97, 115–16 (2013).
133. *See id.*
134. *See generally* Part II, *supra*. *See also* Abbott & Snidal, *supra* note 7; Cafaggi & Renda, *Labyrinth*, *supra* note 3.

operate through domestic legal systems, tethered to and manifesting state

The private regulation movement effectively abandons that project, prescribing instead alternatives to public and democratic governance that elevate market values and actors to governing status. The result is to make regulation an "adjunct to the market," in Polyani's words, and thus to create a global economy in which "social relations . . . [are] embedded in the economic system" rather than the "economy . . . embedded in social relations."[144] As this Article has argued, the case for private regulation is unconvincing because it depends upon ignoring, thereby making invisible, the real and robust role law plays in enabling and protecting MNCs. Bringing that role to light is important not only for revealing the true and disturbing vision underlying private regulation—a world where public power promotes private interests, while public interests depend on private power for protection—but also for making visible the urgent need and many possibilities for finding better ways forward.

144. *See* Muir-Watt, *supra* note 7, at 421; Shamir, *Capitalism, Governance and Authority*, *supra* note 2, at 535 (describing this situation as the "economization of authority").