



Queen Mary University of London, School of Law
Legal Studies Research Paper No. 140/2013

The Nature of Corporate Governance: The significance of national cultural identity

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Preface

The thesis of this book argues that national corporate governance is extremely important for societies. Recently many scholars have said that a convergence of corporate governance is inevitable. We believe that it is true but like Mark Twain said “the report of my death was an exaggeration”. We show that although there is some convergence national law of corporate governance is thriving. We also believe that it is necessary for the identity of each country. The reason that national diversity in corporate governance is still widespread is because of the history, philosophy and economy of each country as shown in its cultural heritage and it gives its identity. The cultural heritage in each state is identifiable in the Company Law and Corporate Governance Codes. We consider that this is crucial for the well being for democratic nations. Convergence in corporate governance is a threat to ordered commercial regulations because of the power of the preeminent economic paradigm in the West which is the neo-liberal model. The neo-liberal agenda that predicates deregulation, privatisation and the liberalisation of markets is moulding many jurisdictions into an Anglo-American model of corporate governance which is dangerous for a number of reasons;¹

- It is an extreme sort of utilitarianism without significant ethical principles
- It allows the growth of mega companies backed by powerful international institutions including the International Monetary Fund (IMF), the World Bank (WB), the Organisation for Economic Cooperation and Development (OECD) and the World Trade Organisation (WTO).
- It changes the balance of power between states, individuals and countries and the mega companies including the financial sector (‘the markets’) and the international institutions.
- It is disastrous because of the burgeoning inequality between nations and individuals
- It is profoundly anti-democratic because of the powerful actors
- It is disastrous for the environment

Against the power of large companies and Multinational Companies (MNEs) and the financial institutions national policy makers are disadvantaged because of the imbalances. Chapter 1 is concerned with global issues coming from the pre-eminence of the neo-liberal agenda. Corporate governance matters because of the sort of society that each state wants. Imbedded in each nation issues of board structures and general

¹ Loraine Talbot *Progressive Corporate Governance for the 21st Century*, **Routledge 2013**.

meetings is the whole structure of the economic management in the country. Western capitalism is always a compromise between ethical principles and pragmatism, God and Mammon, God against the Devil. We will consider in each section the tensions between these concepts in corporate governance. Modern discourse uses different words to express a concept of God. We use terms like human rights, corporate social responsibility, ethical principles, communitare, sustainability, democracy, public interest or bona fide. On the other side there are terms like efficiency, growth, development and necessity. In each chapter of our book we highlight the tension between these powerful ideas and the compromises that policy makers have made in different jurisdictions to reach a balance between them. We contemplate the neo-liberal paradigm as a rigid contractual model as an economic system unable to imagine the value of real equality rather than simulated equality leading to significant consequences. A rigid contractual model will always involve significant advantages for the powerful unless law or regulation can rebalance the equation. The neo-liberal prescription involves a number of crucial tenets, including rigid interpretation of property rights and ownership. In Chapter 1 and 2 we show how important these tenets are although these concepts can be reinterpreted in a different light depending on the historical and philosophic foundation of each nation. We show that property rights and ownership is a chimera or a chameleon.. Property rights are a construct; the definition of ownership and property rights depends on whether there a rigid interpretation of them. A rigid interpretation of them allows special interests to flourish, a looser interpretation of property and ownership allows ethical and communitaire ideas to flourish in corporate governance. In Chapter 5 we consider the German political consensus model which allows a common understanding of the interests of the community including companies. The opposite neo-liberal model is predicated on contract which is a rigidly contractual. We the differences first in Chapter 1 where the different definitions of property rights is starkly exposed when the Indians lost their lands, but thought the book it pervades all of aspects of corporate governance. The stakeholder versus the shareholder debate is about ethical principles versus profit and the ownership of companies is part of this argument. The German consensus of politics is about the ownership of the 'commons', a public interest concept which has resonance in corporate governance. On the other hand the individualism of the American political system with its rigid adherence of property rights is a reason why maximisation of profit is a key part of corporate governance in the US. In the UK there is an uneasy compromise between neo-liberal corporate governance and a stakeholder model embedded in the Company Law 2006 section 172 where there is a fig leaf for stakeholders other than shareholders. Throughout the book we show these tensions between individual shareholders and the public interest in different jurisdictions. We wish to scrutinize the foundation of key concepts of corporate governance because each country understands these concepts slightly differently and if policy makers which to amend the law these tenets need to be thoroughly examined. We hope that this might be particularly useful for policy makers in the transition countries including countries that are apply to join the EU but also when each jurisdiction reviews its corporate governance systems.

Our research shows that although the neo-liberal paradigm is extraordinarily powerful, so much so that many scholars expect that all corporate governance systems will be converged eventually, but there is divergence particularly in important details. The ongoing western recession might trigger a revolution of corporate governance² allowing a stakeholder model to thrive. In the meantime national policy makers need to get the global picture before drafting laws and corporate governance systems which reflects as much as possible the culture of in their county adapting it to the international ‘standards’ promoted by global institutions. Chapter 1 considers the history and philosophy of neo-liberalism and the colonisation of the neo-liberal paradigm on corporate governance particularly and the way that it is promoted in Codes, templates and standards. The contractual model of bargains and companies is discussed showing why a contractual model leads inevitably to inequality. When inequality is predominant that leads to a democratic deficit because of the imbalance between actors. Democracy is not just a matter of voting imbalance between powerful interests are crucial. Trying to balance powerless and the powerful is a fundamental tenet for democracy. A stakeholder model of corporate governance tends to iron out some of the imbalances. There is no doubt that a principal reason for the 2007-2008 financial crash is the imbalance between the financial sector and governments. A bank too big to fail is inevitably a risk because of a conflict of interests between a society. The situation was a moral hazard because the risk of gambling is high. A neo-liberal contractual model followed by the banks allowed them to become powerful because there were not enough checks and balances in the companies. The shareholders wanted the profit, the governments wanted investments in the economy, and other stakeholders were powerless. Eventually this led to bail outs by the taxpayers. We see now the consequences of reckless borrowing which is linked to the bank crisis in the Eurozone. Unfortunately national policy makers can not significantly influence the corporate governance of big banks because the corporate governance of banks is regulated internationally however a system of scrutinizing public companies in each jurisdiction is important to make sure that stakeholders have sufficient information. Environmental protections by companies are become essential because of the need to live sustainably. The threat of climate change is enormous. Here the tensions here are immense because all companies consume resources in their trading and manufacture. Here the neo-liberal theory is particularly dangerous because of its rooted dislike of regulation and simultaneously the ability to use extraterritoriality especially in switching assets between companies. Chapter 2 discusses the convergence and divergence in corporate governance each jurisdiction and why public policies matter. We believe it is crucial to reflect the history, political ideology of each society.

² Dignam, Alan., and Galanis, Michael., *The Globalization of Corporate Governance*, Ashgate, 2009, “the rule of the free-market radicals that started with Margaret Thatcher and Ronald Reagan has ended with a big bang’. If that is so, then the price of that bang will be high, indeed the down payment has already by early 2009 been exorbitant, but perhaps in a more regulated demand managed world, stability and incremental innovation may come to be valued once more over excess profitability and in turn the insider corporate governance model once have its day in the sun, page 419.

Differences matter if communities are to be comfortable and find their identity. In Chapter 2 identifies four streams of corporate governance, of course with many tributaries. Roughly we have identified 1) legal based corporate governance scholarship focusing on shareholder rights, agency problems between shareholders and the management on companies and different models of boards;³ 2) An economic analysis of corporate governance trying to assess the efficiency of different models of company structures;⁴ 3) The debate between the shareholder primacy model versus the stakeholder design of company and whether the models are converging;⁵ 4) A soft-law focus which involves wider issues including ethical principles in companies, including issues of sustainability, corporate social responsibility. This category includes the concession theory of companies⁶. Chapters 3-5 consider the four streams of corporate governance in the context of a detailed knowledge of the structures of companies in the USA, the UK and Germany showing how diverse they are. Amending or drafting company law or principles of corporate governance needs detailed consideration of the structure of boards or the rights of stakeholders while simultaneously considering the cultural identity of each nation.

³ Andenas, Mads and Wooldrige, Frank, *European Comparative Company Law*, Cambridge University, 2009, Plessis du Jean Jacques, Hargovan Anil, Bagaric Mirko, *Principles of Contemporary Corporate governance*, Cambridge University Press, 2011

⁴ **Dignam, Alan and Galanis, Michael, *The Globalization of Corporate Governance*, Ashgate Publishing, 2009,**

⁵ Hansmann, Henry and Kraakman, Reinier, "The End of History for Corporate Law" (2000). Harvard Law School John M. Olin Center for Law, Economics and Business Discussion Paper Series. Paper 280

⁶ For example: Parkinson, J, "The Socially Responsible Company" in Addo, M, (ed) *Human Rights Standards and the Responsibility of Transnational Corporations* Kluwer, The Hague, 1999, Boeger, Nina Rachel Murray, Rachel, and Charlotte Villiers, Charlotte, (Eds.), *Perspectives on Corporate Social Responsibility*, Edward Elgar Publishing, 2008, Keay,A, *The Corporate Objective*, Edward Elgar, 2011

Chapter 1

Corporate governance global economics: the neo-liberalism paradigm.

This Chapter discusses the neo-liberal economic paradigm from several angles. We start with the anxiety that there is a crisis of capitalism because of growing inequalities globally and within countries. We believe that the increasing convergence of corporate governance into a neo-liberal paradigm is one of the causes of growing inequality.⁷ This Chapter traces the historical antecedences of neo-liberalism. We find that it is predicated on contracts which should individually fair but unfortunately bargains are inevitably unequal because of differences between the parties allowing inequality. A rigid adherence of contractual rules does not allow a fair balance between parties where there is stark differences between imbalances of power or riches. The uneven playing field can only be levelled by regulation allowing ethical and communautaire ideas to flourish in corporate governance. We show where the powerful neo-liberal ideas are spreading into international institutions via Codes and international standards influencing other jurisdictions. The World Bank and the OECD are promoters of a number of these initiatives. These initiatives are partly overwhelming the societies who which to adherence a stakeholders model of corporate governance. This is dangerous because if the contractual model of corporate governance become preminent there will be inherent powerful actors able to challenge democratic legitimacy. The Chapter traces the history of the inherent inequality involved in contracts, to the foundation of the contractual model of companies. A contractual model of corporate governance has allowed the flourishing of Multinational Companies (MNEs) which are often more powerful than national governments. The MNEs are helped by international law which shelters them from some risks by structuring their enterprises in a number of jurisdictions. Enforcing harms against MNEs is, extremely complex partly because of the structure of the company veil, international norms and extraterritoriality. The power of the global financial sector is one of the causes of the 2007 financial crisis which is ongoing. We consider the links between the IMF and private banks and which fuelled the Asian crisis of 1997 and the current Eurozone emergency which meant that the taxpayers had to bailout the banks because they were so powerful and so 'big to fail'. The crisis was fuelled by a corporate governance failure; the contractual model of companies was unable to incorporate other stakeholders into

⁷ BBC, 27th January 2012, <http://www.bbc.co.uk/news/business-16757564>, Accessed on 22/01/2013, Jasmine Whitbread, "Will I

Inequality Finally Top the Agenda a Davos, 22/January/ 2013, http://www.huffingtonpost.com/jasmine-whitbread/davos-inequality_b_1235591.html, accessed 22/01/2013.

the model. The accountability of large companies is a threat to democracy not only in a crisis but generally. Democracy is not only about voting, a vibrant democracy does not have actors which are too powerful which undoubtedly MNEs are. The coming risk of pollution and particularly climate change is something that corporate governance policy makers need to consider adapting the structure of companies in a more environmental to encourage sustainability.

The significance of national cultural identity

One would think that the issue of corporate governance would be a purely technical and slightly legalistic one falling within the ambit of what we define rather strictly as company law. Therefore, the issue in question would fall within the interests of mainly academics or corporate lawyers. The truth however is very different. Corporate governance found itself at the very centre of a debate that relates to the very cultural identity and basic political choices made on the part of societies. The fact that corporate governance has provoked a debate which effectively touched upon the fundamental ideological choices of the societies in question clearly revealed the true parameters of the issue and its far reaching effect. The reason behind the debate that has generated hundreds of academic articles and books⁸, a very lively exchange of ideas and opinions on the part of politicians, industry and society and sometimes a rather overt confrontation between important parts of the society such as the employees and the employers is the fact that corporate governance requires the effective engagement of actors that lie at the heart of the most important issues for humanity. To consider 'Corporate Governance' is also to consider competing models of capitalism and competing global economic models. There is no doubt that that we are living in an age when capitalism is in crisis. Many academic commentators believe that there is "a rapidly accelerating and potentially fatal human crisis of global proportions?"⁹ And if there is, are "the systemic forces nurturing the growth and dominance of global corporations . . . at the heart of the current human dilemma?"¹⁰ Escalating recent scandals in the financial sector,

⁸ Riley.A. C, 'Understanding and Regulating the Corporation' (1995) 58(4) *Modern Law Review* 595, 595; Stiglitz, J.E. 'Multinational Corporations: Balancing Rights and Responsibilities' (2007) 101 *Proceedings of the Annual Meeting (American Society of International Law)*, Attenborough D., 'Giving Purpose to the Corporate Purpose Debate: An Equitable Maximisation and Viability Principle' 32(1) *Legal Studies* 4. Parkinson, J.E *Corporate Power and Responsibility: Issues in the Theory of Company Law* (Clarendon Press, 1993) at 237. Keyes, Andrew, *The Corporate Objective*, Edward Elgar, 2011. Cheffins, B, *Company Law : Theory, Structure and Operation* (Clarendon Press, 1997) at 1999, Bottomley, S, *The Constitutional Corporation* (Ashgate, 2007),

⁹ Korten , D *When Corporations Rule the World*, Kumarian Press, 1995, p3

¹⁰ Korten *When Corporations Rule the World* p9.

press manipulation of communications¹¹, the increasing anomie in our societies, the burgeoning inequality between individuals and between states shows that our model of capitalism is in trouble. Rowan Williams argues that “no-one can any longer regard the free markets as a natural beneficent mechanism.”¹²

If there is a crisis of capitalism today it is important to consider the root causes of the problems, economically, philosophically and legally. It is not good enough to divide specialities into watertight compartments. Many scholars argue that powerful companies are a central part of a system which exacerbates poverty and inequality.¹³ “The world has become a dangerous unequal place – even for the rich¹⁴ in the major cities of the West. Debt services alone accounts for \$200 billion a year in currency flows from the South to the North. . . . While 1.2 billion people – nearly a fifth of the world’s population – have to manage on less than a dollar a day”¹⁵, The first decade of this century has not revealed a better world for the poor; rather research shows that inequality has been rampant,¹⁶ and studies suggesting that powerful companies should have responsibilities to the planet and to stakeholders other than shareholders are now legion.¹⁷ However, there are comparatively few arguments¹⁸ linking these problems to the structure of company law and corporate governance itself. The

¹¹ www.levesoninquiry.org.uk/, accessed on 26/9/2012.

¹² Interview by Hare, David with Rowan William, Guardian 9/7/2011.

¹³ Dine, J, *Companies, International Trade and Human Rights*, CUP 2005, Clapham, A, “The Question of Jurisdiction under International Criminal Law over Legal Persons” in Kamminga, M and Zia-Zarifi S, (eds), *Liability of Multinational Corporations under International Law. The Hague: Kluwer. 2000*, Bakan, J, *The Corporation: the Pathological Pursuit of Profit and Power*, New York, Free Press, 2004.

¹⁴ UNDP, *beyond Scarcity; Power, Poverty and the global water crisis*, Human Development Report 2006.

¹⁵ Beck, Ulrich, *Power in the Global Age*, Polity, Press 2005, pages 24-5.

And see Green, Duncan, *From Poverty to Power*, Oxfam. 2008/9, Stiglitz, J, *The Price of Inequality*, Allan Lane, Penguin, 2012, Wilkinson, Richard and Pickett, Kate, *The Spirit Level*, Penguin, 2009 and 2010.

¹⁶ <http://www.worldhunger.org/articles/Learn/world%20hunger%20facts%202002.htm>, www.oxfam.org.au/refugee/public/issues/.../statistics.php, United Nations Development Programme Report 2010, Both accessed on 28/7/2012.

¹⁷ For a few see: John Ruggie, Human Rights Council, Seventeenth session, “Report of the Special Representative of the Secretary-General on the issue of human rights and transnational corporations and other enterprises” A/HRC/17/31, Zerk, Jennifer, *Multinational and Corporate Social Responsibilities: Limitations and Opportunities in International Law*, CUP, 2006, Eroglu, Muzaffer, *Multinational Enterprises and Tort Liabilities*, Edward Elgar, 2008, Boeger, Nina Rachel Murray, Rachel, and Charlotte Villiers, Charlotte, (Eds.), *Perspectives on Corporate Social Responsibility*, Edward Elgar Publishing, 2008,

¹⁸ But see Dignam, Alan and Galanis, Michael, *The Globalization of Corporate Governance*, Ashgate Publishing, 2009, Zerk, Jennifer, *Multinational and Corporate Social Responsibilities: Limitations and Opportunities in International Law*, CUP, 2006, Eroglu, Muzaffer, *Multinational Enterprises and Tort Liabilities*, Edward Elgar, 2008,

links between company law and corporate governance, deepening poverty and the structure of company law have not yet been fully drawn. Add the multifaceted environmental¹⁹ crisis, including climate change and pollution means that we need to question all of our institutions, including companies and the related issue of corporate governance. Companies are not a natural phenomenon they were crafted by societies whether by individuals or together in regional pacts (like the European Union (EU)) and influenced by global players like the International Monetary Fund (IMF), the World Bank (WB), the World Trade Organisation (WTO)²⁰ or Organisation for Economic cooperation and Development (OECD). Their behaviour and structures must be examined and scrutinised. This book charts details of corporate governance in the United States of America (USA), United Kingdom (UK) and Germany. It is not possible to consider *all* of the *global* influences which have led to the current international system of corporate governance, however, there is a pressing reason to examine four issues; the international neo-liberal economic model, international inequality, democracy, and (briefly) the negative impact on the environment. To examine Corporate Governance without considering these would be negligence. The thesis of this book is that national policy makers should be supported from powerful companies and the international institutions which promote them. Corporate governance laws and codes should be drafted with democracy in mind, considering the national history and philosophy. Democracy will never thrive if rich agents are able to subordinate citizens. Our research shows that although the neo-liberal paradigm is extraordinarily powerful, so much so that many scholars expect that all corporate governance systems will be converged eventually, there is divergence particularly in important details. The ongoing western recession might trigger a revolution of corporate governance²¹ allowing a stakeholder model to thrive. In the meantime national

¹⁹ Hulme, Mike *Why We Disagree about Climate Change*, Cambridge University Press, 2009, Barbier, Edward B., *A Global Green New Deal*, United Nations Environment Programme (UNEP), 2010, www.unep.org/, accessed 25/10/2012, Helm, Dieter and Hepburn, Cameron (Eds), *The Economics and Politics of Climate Change*, Oxford University Press 2009, Stern, Nicholas, *The Economics of Climate Change*, Cambridge University Press, 2008. Chossudovsky, M., *The Globalisation of Poverty*, Pluto, Halifax, Nova Scotia, 1998, Harrison, P., *Inside the Third World*, (3rd ed) Penguin, Harmondsworth 1993, Hertsgaard, M., *Earth Odyssey*, Abacus, London 1999, Karliner, J., *The Corporate Planet*, Sierra Club, San Francisco 1997, *Oxfam Global Finance, Tax Havens: Releasing the Hidden Billions for Poverty Eradication*, Oxfam, Boston, 2001, <http://policy-practice.oxfam.org.uk/our-work/aid-development-financ>, accessed on 25/10/2012, and *Oxfam America Oil gas and mining: Poor Communities Pay the Price*, Oxfam, 2001 Boston, Redclift, Michael, and Benton, Ted (eds) *Social Theory and the Global Environment*, Routledge, 1994.

²⁰ Dignam, Alan., and Galanis, Michael, "Corporate Governance and the Importance of Macroeconomic Context", *Oxford Journal of Legal Studies* 28, (2008), 201.

²¹ Dignam, Alan., and Galanis, Michael., *The Globalization of Corporate Governance*, Ashgate, 2009, "the rule of the free-market radicals that started with Margaret Thatcher and Ronald Reagan has ended with a big bang". If that is so, then the price of that bang will be high, indeed the down payment has already by early 2009 been exorbitant, but perhaps in a more regulated demand managed world, stability and incremental innovation may come to be valued once more over excess profitability and in turn the insider corporate governance model once have its day in the sun, page 419.

policy makers need to get the global picture before either only considering national corporate governance in a watertight compartment which is now almost impossible or drafting laws and corporate governance which reflects as much as possible the culture of in their county adapting it to the international ‘standards’ promoted by global institutions. However we start with considering the dominant economic model, the neo-liberal paradigm.

The Neo-Liberal Economic Model

“In the old political game of ‘national (welfare)’ the aim was to achieve the greatest possible security . . . against a background of national homogeneity, . . . The neo-liberal agenda is an attempt to capture the momentary historical gains of global and political mobile capital and fix them institutionally . . . according to this scheme, what is good for capital is good for all: everyone will be get richer, and ultimately even the poor will benefit, or so the promise goes. The seductiveness this neo-liberal ideology, then, lies not in giving selfishness a free rein or in maximizing competition, but in the promise of global justice. The implication is: maximizing the power of capital is *ultimately* the better way towards socialism. *That* is why the (welfare) state is superfluous²². The neo-liberal philosophy “allocates to states the function of a guardian of free, spontaneous markets through the instrumentality of the ‘rule of law’²³. The foundation of this theory is suspect for many reasons, including the concept of the ‘rule of law’ which can be bent into a number of shapes.²⁴ The neo-liberal economic paradigm was first invented by the Chicago University economists, the so-called Milton Friedman ‘Chicago Boys’ who were recruited by the Central Intelligence Agency (CIA) to help with the reconstruction of the Chilean economy following the Pinochet coup in 1973²⁵ Although Milton Friedman is the author of the modern neo-liberal school, there is a long tradition of right wing scholars who wanted to disparage the state and promote markets. Skidelsky and Skidelsky²⁶ traces the history of the neo-liberal paradigm back to the enlightenment philosophers who believed that man (not women, of course) were rational²⁷. They propounded a theory of utilitarianism. Skidelsky and

²² Beck, U., *Power in the Global Age, Polity, 2005, pages 4-5*

²³ Birch, Kean., and Mykhnenko, Vlad *Introduction., – A World Turned Right Way Up* in Birch, Kean, & Nykhnenko Vlad (eds) *The Rise and Fall of Neo-liberalism: The Collapse of an Economic Order?*, Zed Books 2010, page 3.

²⁴ Tamanaha, Brian., Cambridge University Press, 2004, arguing that should be a universal norm for the benefit for humankind.

²⁵ Klein, Naomi., *The Shock Doctrine: The Rise of Disaster Capitalism* (Allen Lane 2007) 7, 25-38

²⁶ Skidelsky R., and Skidelsky E., *How Much is Enough?*, Allen Lane, 2012.

²⁷ Schous, Peter A., *Reasoned Freedom*, Cornell University Press, 1992.

Skidelsky use the ‘Faustian Bargain’ fable to illustrate the point. The issue was that utilitarian theories can be good for economic growth but often the instruments that are used are immoral. In Christopher Marlowe’s play Dr Faust lost his soul.²⁸ Some other authors augmented the fable to allow Faust to go to heaven because he did good deeds, now this is what is meant as a ‘win-win situation! “By the early nineteenth century, in Goethe’s classic retelling (1808 and 1832) Faust has become a symbol of endlessly striving modern man, fallible but ultimately worthy of love. Goethe’s *Faust* can be seen as the literally expression of the *felix culpa* of the political economist. With the help of Mephistopheles, Faust does all of kinds of terrible, but at the end his soul goes to heaven because he has ‘striven greatly’. Faust’s elevation from wicked prankster to world-historic hero reflects the weakening of Christian orthodoxy and its absolute prohibition on evil. It insinuates the heretical thought that in our dealing with the Devil it is *we* who can come off winners”²⁹ Keynes was also ambivalent about capitalism saying that “It was a civilization which unleashed bad motive for the sake of good results. Morality had to be put in cold storage till abundance was achieved, for abundance would , make possible a good life for all”³⁰ Keynes wrote “we must pretend to ourselves and to every one that fair is foul and foul is fair; for foul is useful and fair is not. Avarice and usury and precaution must be our god for a little longer still. For only they can lead us out of the tunnel of economic necessity into daylight”³¹ The Skidelskys show us that Christian theology had a simple dichotomy of evil and good, but this was lost when the Reformation softened the orthodoxy³² This allowed utilitarianism doctrines to be followed without retribution by the devil. , “The Renaissance invented – or rediscovered – the idea of *using* human desires to govern societies rather than castigating them as wicked. The wise prince, wrote Machiavelli³³, threats people as they are, not as they should be: he exploits their fickleness, hypocrisy and greed to attain his ends”³⁴ Both doctrines are simplistic because we now know much more about the human brain and the complexity of the networks connecting the desires and emotions in the human mind³⁵. However the dichotomy of evil and good continues to be a powerful narrative and against this utilitarian theories were propounded by

²⁸ Marlowe, Christopher.,*The Tragical, History of the Life and Death of Doctor Faustus*, 1604.

²⁹ Skidelsky and . Skidelsky *How Much is Enough?*, Allen Lane, 2012, page 55.

³⁰ . Skidelsky and . Skidelsky *How Much is Enough?*, Allen Lane, 2012, page 43.

³¹ Maynards, Keynes., John, *Essays in Persuasion, The Collected Writings of John Maynard Keynes*, Yol 9, Cambridge University Press, 1078. Page 372, and see . Skidelsky R, *Keynes; The Return of the Master*, Penguin, 2009. , ,

³² . Skidelsky and . Skidelsky *How Much is Enough?*, Allen Lane, 2012, page47.

³³ Machiavelli, Niccolo., *The Florentine History*, . Charleston,S.C, Forgotten Books, 2010, vol.2.

³⁴ . Skidelsky and . Skidelsky *How Much is Enough?*, Allen Lane, 2012, page47.

³⁵ Eagleman, David., *Incognito: The Secret Lives of the Brain*, Cannongate, 2011, particularly Chapter 5 ‘The Brain as a team of rivals’ where the author posits the idea that the brain is similar to a democracy.

merchant class who found a powerful voice in Bernard Mandeville (1670-1733). The Skidelskys cite Mandeville's best-known work, the *The Fable of the Bees, or the Private Vices, Publick Benefits*, "Mandeville's bees are addicted to 'Fraud, Luxury and Pride', yet succeed, through 'State's Craft', in transforming these 'private vices' into the public benefit' of commerce and industry:

The Root of Evil, Avarice,
That damn's ill-nature's baneful Vice
Was Slave to Prodigality,
That Noble Sin; whilst Luxury
Employ'd a Million of the Poor,
And odious Pride a Million more:
Envy it self, and Vanity,
Were Ministers of Industry"³⁶

The authors show us how vice is slowly turned into a colourless sin by a with breathless public relations coup into self-interest. The stage is set for Adam Smith's *The Wealth of Nations*.³⁷ The Skidelskys argue that the paradigm shift was possible because Adam Smith presents "humans as driven by natural desire from self-improvement, which under conditions of free competition leads them 'as if an invisible hand' to promote the public well-being. . . . This was a revolutionary invention. Traditional morality had conceived of society as an enterprise devoted to the common good . . . Smith's doctrine of self-interest did more than just turn avarice into a virtue; it turned classical virtue into a vice. . . In Smith's political economy, asceticism becomes the virtuous form of self-interest, the efficient cause of capital accumulation. Alms-giving was discouraged because it promotes idleness"³⁸ The theology of the beatitudes was eclipsed "Thou shalt love thy neighbour"³⁹ was redundant. Utilitarian doctrines are very dangerous as Pogge writes "moral norms, designed to protect the

³⁶ . Skidelsky and . Skidelsky *How Much is Enough?*, Allen Lane, 2012, page49.

³⁷ Smith, Adam, *The Wealth of Nations*, Prometheus Books, 1991(originally published in 1776)

³⁸ . Skidelsky and . Skidelsky *How Much is Enough?*, Allen Lane, 2012, page 50, and see the recent debate in the UK, especially by right-wing Conservative politicians, Kwarteng, Kwasi Patel, PritiDominic Raab, Dominic Skidmore, Chris, and Truss, Elizabeth *Britain Unchained*, Palgrave Macmillan, 2012, Stiglitz, J, *The Price of Inequality*, Allen Lane, Penguin, 2012, especially, page229.

³⁹ St Mathew, Chapter 5, verse 43 although the Puritans were ambivalent about capitalism, see Sedgwick, Peter H, *Christian Ethics*, Cambridge University Press, 1999

livelihood and dignity of the vulnerable, place burdens on the strong. If such norms are compelling enough, the strong make an effort to comply. But they also, consciously or unconsciously, try to get around the norms by arranging their social world so as to minimise their burdens of compliance.”⁴⁰ The utopian vision of a win-win situation is a rosy vision but it is not reality. Instead the neo-liberal theology has given us multinational companies which are so powerful that governments are nearly powerless⁴¹. Neo-liberal economic theory is the dominant force fuelling the convergence theory which says that all company governance should be run on the Anglo-American, contractual model⁴². For multinationals and their subsidiaries it is efficient in monetary terms, but significantly flawed, leaving many externalities in its wake. One of the externalities is the erosion of democracy. This is why Beck⁴³ realises that not only has power shifted from governments and people and also that ethical principles are absent including justice.⁴⁴: An excellent synopsis of neoliberalism is found in Glinavos:

“How, then, did a specifically neoliberal version of capitalism built on an essentially American model of ‘laissez-faire’ become the strand of western free market ideology that won the day. . . [this has become] the theoretical underpinnings of neoliberalism, focusing in particular on its underlying assumptions that markets are natural; that the rationality of their operations is threatened by governments intervention ; that the role of law is limited ; that law should be subordinate to markets needs; that the ‘invisible hand’ of the market not only ensures efficiency but also distributive justice.”⁴⁵

⁴⁰ Pogge T, *World Poverty and Human Rights*, Polity, 2002 and 2008, p5

⁴¹ Ainger, Katherine, “A Financial Coup D’etat: The Spanish government may be happy to sacrifice sovereignty for a bailout. But not the Indignos”, *Guardian* Wednesday 26/09/2012.

⁴² Hansmann, Henry and Kraakman, Reinier, "The End of History for Corporate Law" (2000). Harvard Law School John M. Olin Center for Law, Economics and Business Discussion Paper Series. Paper 280 but see a powerful contra argument by Andrew Keay, *The Corporate Objective*, Edward Elgar, 2011 and J. Parkinson “The Socially Responsible Company” in Addo, M, (ed) *Human Rights Standards and the Responsibility of Transnational Corporations* Kluwer , The Hague, 1999

⁴³ Beck *Power in the Global Age*, Policy Press, 2005.

⁴⁴ Green, *From Poverty to Power*, Oxfam, 2008, . Kwa, A, *Power Politics in the WTO*, Focus on the Global South, Jan 2003, Dine, *Companies, International Law and Human Rights*, Cambridge University Press, 2005, especially chapter 3.

⁴⁵ Glinavos Ioanni *Neoliberalism and the Law in Post Communism Transition*” Routledge 2010, page 12.

The recent history of neo-liberal is to found in the scholarship propounded by the Austrian economist and social philosopher, Ludwig Von Mises and Friedrich Von Hayek.⁴⁶ Von Mises's axiom that 'egoism is the basic law of society'⁴⁷ led him to conclude that unrestricted laissez-faire, free markets and governments that are confined to the defence of unhampered private property rights comprised the only viable policy for the human race.⁴⁸ The neo-classicist doctrine is that that rational actors will, if left undirected, make maximally efficient economic decisions which will maximise their welfare, leading to an efficient economy where all will eventually benefit: "For more than 20 years economists were enthralled by so-called "rational expectations" models which assumed that all participants have the same (if not perfect) information and act perfectly rationally, that markets are perfectly efficient, that unemployment never exists (except when caused by greedy unions or government minimum wages) and where there is never any credit rationing."⁴⁹ That this model is becoming increasingly discredited does not alter the fact that faithful adherents in this model are acting on the theory and now it is the dominant economic paradigm for the world: "At the time of writing, markets have assumed mythological proportions. Like the Gods of ancient days, their displeasure looms over popular protestations. In places such as Greece and Italy, governments stand or fall by their ability to respond to divine dictates. Translated into modern discourse, what is being witnessed is the practice of neoliberal national and transnational governance."⁵⁰ The consequences are dire for the populations of these countries'⁵¹, the denigration of the environment and increasing inequality but as well as this the decrease of democracy, including the hollowing out national states "The neo-liberal regime provides for globally binding decisions against individual states' resistance, and a universally valid and application 'policy mix' is propagated accordingly. This means that political reforms should be oriented towards economic objectives – low inflation, a balanced budget, the removal of trade barriers and foreign currency controls, maximum mobility for capital minimum regulation of the labour market and a lean, adaptable welfare state that orders its citizens to work. There are the *the* reform objective of the neo-liberal regime . . . it is supposed to be apolitical but of course it is highly political"⁵² This project has fundamental

⁴⁶ Birch & Mykhnenko, *The Rise and fall of Neo-Liberalism: The collapse of an Economic Order*, Zed Books, 2010, page 3.

⁴⁷ *ibid*

⁴⁸ Murray N. Rothbard, 'Biography of Ludwig Von Mises (1881-1973)' Ludwig Von Mises Institute <<http://mises.org/about/3248>> accessed August 16th 2012..

⁴⁹. Stiglitz, J Guardian, Friday December 20th 2002, and see . Stiglitz, J, *The Price of Inequality*, Allen Lane, Penguin, 2012

⁵⁰ Rercival, Yonit, Phd forthcoming, Queen Mary, University of London, 2012

⁵¹ Hellenic Observatory, European Institute, "The Greek Crisis in focus, Austerity, Recession and the path to Recovery, <http://www2.lse.ac.uk/europeanInstitute/research/hellenicObservatory/pdf/GreeSE/GreeSE%20Special%20Issue.pdf>. Accessed on 21/8/2012, GlobalPost, "Greek unemployment soars with one fifth out of work <http://www.globalpost.com/dispatch/news/business-tech/debt-crisis/120412/greek-unemployment-soars-over-one-five-out-work>, accessed on 21/8/2012.

⁵² Beck, *Power in the Global Age*, page 79.

consequences for corporate governance because of the idea that convergence of systems of corporate governance is inevitable. It is clear that corporate governance ‘reforms’ follows the neo-liberal agenda orchestrated by powerful institutions including the World Bank and The Organisation for Economic Co-operation and Development (OECD): “As part of the Reports on the Observance of Standards and Codes (ROSC) initiative, the World Bank has established a program to assist its member countries in strengthening their corporate governance frameworks. The objectives of this program are to

- Benchmark the country’s corporate governance framework and company practices against the OECD Principles for Corporate Governance.
- Assist the country in developing and implementing a country action plan for improving institutional capacity with a view to strengthening the country’s corporate governance framework.
- Raise awareness of good corporate governance practices among the country’s public and private sector stakeholders.

Promoting the neo-liberal agenda in corporate governance: standards, codes and templates

The World Bank conducts corporate governance country assessments under the Reports on the Observance of Standards and Codes (ROSC) initiative at the invitation of country authorities. The World Bank uses a diagnostic tool – a Template - that it has developed to gather pertinent information for preparing the Corporate Governance ROSC.”⁵³ It is very clear that the World Bank Template of Corporate governance is significantly tilted against stakeholders other than shareholders; the Template propagates the canard⁵⁴ that the shareholders are the owners⁵⁵ of the company.⁵⁶ The Template considers the most important issues of corporate governance to be the rules about shareholders’ rights and particularly their property rights. The Template is in a form of a questionnaire and the first section is entitled “Ownership and Control” question 1 about the “ownership and its concentration”⁵⁷. Later in

⁵³ http://www.worldbank.org/ifa/rosc_cg.html, accessed on 17th/8/2012.

⁵⁴ Ireland, P, “Company Law and the Myth of Shareholder Ownership” 1999 MLR 62, See also J. Hill “Visions and Revisions of the Shareholder” (2000) American Journal of Comparative Law 39.

⁵⁵ Key, *The Corporate Objective*, Edward Elgar, 2011, considering this issue several times including when he cites the UK’s Cadbury committee in its *Report on the Financial Aspect of Corporate Governance*, page 66, and see the ownership debate Chapter 2..

⁵⁶ See Chapter 2 on this point.

⁵⁷ http://www.worldbank.org/ifa/CG_template.pdf, accessed on 20/8/2012

this template a key concept of neo-liberal axioms appears, that is the message that markets should be 'efficient' without properly defining efficiency: it is certain that the template prefers a shareholder primacy or insider model.⁵⁸ On these terms many externalities are not included in the definition of 'efficiency', especially a fair wage for employees. "A Corporate governance framework should be developed with a view to its impact on overall economic performance, market integrity and the incentives it creates for the market participants and the promotion of transparent efficient markets."⁵⁹ Chapter II details the importance of shareholders' rights "The title is 'The rights of shareholders and key ownership functions': The corporate governance framework should protect and facilitate the exercise of shareholders' rights".⁶⁰ The questions in this section are extensive, involving questions 141-201 after this there is a wide-ranging set of questions about the market for corporate controls which is neo-liberal speak for takeovers which allows the powerful companies to dominate the international agenda and often dominate states⁶¹: "Markets for corporate control should be allowed to function in an efficient and transparent manner."⁶² (19 questions). Chapter III returns to the equitable treatment of shareholders' rights with (another 31 questions). The template only mentions stakeholders at question 277 where Chapter V deals with stakeholders: "Do any laws provide rights to stakeholders (employees, trade unions, creditors, customers, suppliers, consumers, and the community) to participate or have input in the corporate governance of the company?". Although the section is headed 'Stakeholders' it is telling in its definition; it "includes constituencies *other than shareholders*"⁶³, such as employees, trade unions, creditors, customers, suppliers, consumers, and the community."⁶⁴ The divisions between 'stakeholders and shareholders are very glaring. Shareholders are a privileged class, not part of the company's' community, the template clearly classify the lambs and the goats, and as well as this evidently the shareholders are 'owners' and the rest of the stakeholders of the enterprise are not part of the polity. It is interesting that the term 'corporate social responsibility' is not included although many scholars believe that the convergence of corporate social responsibility and corporate governance is one of the ways

⁵⁸ See later on the definitional of these terms.

⁵⁹ http://www.worldbank.org/ifa/CG_template.pdf, accessed on 20/8/2012

⁶⁰ http://www.worldbank.org/ifa/CG_template.pdf, accessed on 20/8/2012

⁶¹ See later on the takeover debate.

⁶² http://www.worldbank.org/ifa/CG_template.pdf, accessed on 20/8/2012

⁶³ My italics.

⁶⁴ http://www.worldbank.org/ifa/CG_template.pdf,question 277, accessed on 20/8/2012

that accountability and responsibility in companies could be fostered. Responsible capitalism and neo-liberal capitalism are at odds. Corporate Governance and Corporate Social Responsibility(CSR) is where competing philosophies divide. To illustrate this divide is to look at the OECD's Corporate Governance Code (2004) and the OECD Guidelines for Multinational Enterprises (2011) which are significantly different and, some would say, contradict themselves⁶⁵. The OECD's Corporate Governance Code is about regulating the internal management of companies; the Guidelines are concerned about external pressures on companies including ethical, social and environmental issues. This part of this book shows why these two competing Codes should be aligned by considering the risk for companies who ignore externalities, external stakeholders and the wider community. This means contemplating global issues, ethical and intergenerational externalities which should be internalised by companies. Zerk argues that CSR and Corporate Governance are distinct but related; "It is not surprising, but these are actually two separate concepts. Corporate governance is generally taken to refer to issues relating to ownership and control of companies, and covers topics such as decision-making, reporting and transparency, whereas CSR, . . . is concerned with a wider sets of relationship – with employees, suppliers, communities, consumers and interested NGOs."⁶⁶ In *Companies, International Trade and Human Rights*⁶⁷ Dine attempted to show that Corporate Governance, Corporate Social Responsibility, property rights and risks are symbiotic terms, all of these terms are bound in with the way that society orders its economic and its justice. It is very distressing that the discipline of corporate governance is often considered as a separate speciality from CSR. If the two concepts are to be merged much research is necessary to implement concrete proposals,⁶⁸ turning it into a solid foundation from which legislators can draft company laws rather than vague statements like those appearing in the Code. Further, having identified society's concessional boundaries,⁶⁹ these need to be fed into the decision making machinery of a company and extracted from the public relations⁷⁰ departments of companies. In Chapter 5 the authors argue that in a small way this could be done by drafting a law which could allow government and individual to sue multinational companies in their own jurisdiction

⁶⁵ The sources rely on the earlier version of the Guidelines: . Chatterjee, C "The OECD Guidelines for Multinational Enterprises: an analysis" 2002 *Amicus Curiae* 18. . Karl, J, : "The OECD Guidelines for Multinational Enterprises" in .Addo, M, (ed) *Human Rights Standards and the Responsibility of Transnational Corporations*", Kluwer 1999.

⁶⁶ Zerk, *Multinationals and Corporate Responsibility*, CUP, 2006, page 31.

⁶⁷ Dine, CUP, 2005

⁶⁸ The Ruggie report is trying to 'operationalizing' principles which are central to company governance and human rights, <http://198.170.85.29/Ruggie-report-2010.pdf>, accessed on 28/09/2012.

⁶⁹ See later considering the concession theory and Chapter 5.

⁷⁰ Tench, Palph, and Yeoman,Liz, *Exploring Public Relations*, Pearson, 2012.

including foreign subsidiaries. If this could be done in some jurisdictions there could be a significant change of culture allowing better accountability for powerful companies. .

Synergies and disparities between the OECD Guidelines for Multinational Enterprises (the Guidelines) 2011 ⁷¹ and Principles of Corporate Governance 2004 ⁷²

If Corporate Governance should be about an ethical framework for companies including how companies can be expected to comply with laws and soft law initiatives, a vital step in making corporate governance norms effective is to marry corporate governance codes with ethical principles.

At present those concerning themselves with the *methods* of decision making within companies and the enforcement mechanisms to ensure proper decision making appear to be inhabiting a different planet from those drawing up guidelines and codes of conduct. Principally the neo-liberal ‘governance’ debate accepts the primacy of shareholders whereas many CSR Codes have been extended far into stakeholder territory without concerning itself with how implementation may change the governance rules. The disparities between the OECD *Guidelines for Multinational Enterprises (the Guidelines) 2011* ⁷³ and *Principles of Corporate Governance 2004* ⁷⁴ (the Principles) can certainly be seen in this light. The Articles of the OECD Convention promotes policies designed

“– to achieve the highest sustainable economic growth and employment and a rising standard of living in member countries, while maintaining financial stability, and thus to contribute to the development of the world economy;

– to contribute to sound economic expansion in member as well as non-member countries in the process of economic development; and

– to contribute to the expansion of world trade on a multilateral, non-discriminatory basis in accordance with international obligations.”

For those who believe that this is impossible because of the constraints of the limits of the planet’s resources’, this is not a good start. If growth is to be limited for reasons of sustainability, this principle should be integrated into corporate governance.⁷⁵ After this the

⁷¹ www.oecd.org/.../0,3746,en_2649_34889_2397532_1_1_1_1,00.ht..., accessed on 22/8/2012.

⁷²

<http://www.oecd.org/daf/corporateaffairs/corporategovernanceprinciples/oecdprinciplesofcorporategovernance.htm>, accessed on 22/8/2012

⁷³ www.oecd.org/.../0,3746,en_2649_34889_2397532_1_1_1_1,00.ht..., accessed on 22/8/2012.

⁷⁴

<http://www.oecd.org/daf/corporateaffairs/corporategovernanceprinciples/oecdprinciplesofcorporategovernance.htm>, accessed on 22/8/2012

⁷⁵ Meadows, Donella, Randers, Jorgen, Meadows, Dennis, *Limits to Growth*, Earthscan, 2010. ,

issue is how the resources should be distributed and this is where corporate governance principles should start to incorporate the key elements of the *Guidelines* especially the concept of sustainability.

The *Principles* are the foundation of the World Bank Template which has been already considered showing the provenance of the ideas. This section analyses the *Principles* and the *Guidelines*. Both start from the premise that “One key element in improving economic efficiency is corporate governance”.⁷⁶ The *Principles* also commences with “the Rights of Shareholders”,⁷⁷ contains the principle that “markets for corporate control should be allowed to function in an efficient and transparent manner”⁷⁸ and “Anti take-over devices should not be used to shield management from accountability”.⁷⁹ The 2000 formulation only nodded to such ‘stakeholders’ as are “established by law”⁸⁰, the 2004 has changed this expanding the ‘stakeholder section’ and increasing the rights of stakeholders by recognising mutual agreements,⁸¹ However there is no prescription as to which constituencies should be regarded as stakeholders. The 2000 formulation said “The degree to which stakeholders participate in corporate governance depends on national laws and practices, and may vary from company to company as well.”⁸² This has been dropped in the version of the *Principles 2004*⁸³ and stakeholders have a slightly enhanced status:

“A key aspect of corporate governance is concerned with ensuring the flow of external capital to companies both in the form of equity and credit. Corporate governance is also concerned with finding ways to encourage the various stakeholders in the firm to undertake economically optimal levels of investment in firm-specific human and physical capital. The competitiveness and ultimate success of a corporation is the result of teamwork that embodies contributions from a range of different resource providers including investors, employees, creditors, and suppliers. Corporations should recognise that the contributions of stakeholders constitute a valuable resource for building competitive and profitable companies. It is, therefore, in the long-term interest of corporations to foster wealth-creating cooperation among stakeholders. The governance framework should recognise that the interests of the corporation are served by recognising the interests of stakeholders and their contribution to the long-term success of the

⁷⁶ OECD Code, Preamble.

⁷⁷ OECD Code, Principle IA

⁷⁸ OECD Code Principle I IIE

⁷⁹ *ibid*

⁸⁰ OECD Code, Principle IV A.

⁸¹ OECD Code, Principle IV A.

⁸² OECD Code Principle III D.

⁸³ OECD Code, Principle IV A.

corporation”⁸⁴. As we argued earlier the *Principles* and also the *OECD Template for Country Assessment of Corporate Governance*⁸⁵ are intended to promulgate the UK/US neo-classical model of corporate governance.

They envisage a model of corporation law;

- 1) which relies heavily on the fiction of shareholder control over management
- 2) adopts the view that shareholder control over management will in some way be beneficial rather than simply increase the pressure for profit maximisation at all costs
- 3) adopts the ‘market forces’ model of ownership control; this model would limit or prevent the adoption of corporate structures mentioned elsewhere in the Code such as the representation of employees on boards and hinder takeovers.⁸⁶ Although the *Principles* does recognise employee participation, in a significant shift from the earlier version, however this change is therefore baffling and incoherence given the neo-liberal tenor of the document. The 2004 version is also more employee friendly; “Examples of mechanisms for employee participation include: employee representation on boards; and governance processes such as works councils that consider employee viewpoints in certain key decisions”⁸⁷

From the international perspective the most glaring omission in this document is the absence of any recognition that a drive for economic efficiency on an international basis is at the root of many of the malpractices in which transnational corporations have been implicated.⁸⁸ Indeed the excessive reliance on the existing models of corporate governance in member states could be seen as using subsidiary principle to shirk the responsibility to suggest best practice so far as the adoption of governance models. In that respect, it is extremely interesting that “Corporate governance is only part of the larger economic context in which firms operate that includes, for example, macroeconomic policies and the degree of competition in product and factor markets”. A clear distinction is drawn between ethical and societal concerns and commercial objectives of companies. Ethical concerns seem to be the last issue: “In *addition*⁸⁹, factors such as business ethics and corporate awareness of the environmental and societal interests of the communities in which a company operates can also have an impact on its reputation and its long-term success”.⁹⁰ ; Both the international dimension and the ‘ethical, environmental and other issues’ are treated more explicitly in the OECD Guidelines for Multinational Enterprises. The two documents read very differently. While neither document purports to be legally binding, the extreme difference of tone may perhaps be explained by the distinction between the suggested standards (Guidelines) and the methods of achieving those (Principles of Corporate Governance). Because of an underlying philosophical difficulty in the structure of the marketplace, there is an insufficient match

⁸⁴ OECD Code, Principle IV, introduction.

⁸⁵ *OECD Template for Country Assessment of Corporate Governance* 2007.

⁸⁶ Co-determination has long been accepted as a barrier to takeovers. See Dine, J, and Hughes. *PE Company Law*, Jordans, looseleaf, Chapter 12, esp 12.19.

⁸⁷ OECD Code, Principle IV, C.

⁸⁸ Dine, J, *The Governance of Corporate Groups*, Cambridge University Press, 2000, P. Muchlinski *Multinational Enterprises and the Law*, Blackwell, 1995.

⁸⁹ My italics.

⁹⁰ OECD Code, preamble

between the exhortations to achieve moral probity and the suggested governance methods. The Guidelines were written in 2000 and reviewed on 2011. There is shift on emphasis in the 2011 text. The both versions still adheres to the attitude that “suggests that the Member Countries may have a moral duty to ensure that the activities of their MNEs in host states *do not contribute* to the detriment of those states’ economies, particularly if they are less developed”⁹¹ However the 2000 Guidelines were mostly negative; trying to limit the damage that the enterprises are doing but at the same time trying to economic growth in the develop nations *and* in the developing countries. Thus “The common aim of the governments adhering to the Guidelines is to encourage the positive contributions that multinational enterprises can make to the economic, environmental and social progress and to minimise the difficulties to which their various operations may give rise”.⁹² I small positive note is struck in supporting sustainability. In particular, the processes are to take place within the framework of “sustainable development”. The puzzle is why there are two documents rather than one and the answer may be of more fundamental importance than would first appear. If the standards articulated in the Guidelines are to be delivered, this can surely only be through corporate governance mechanisms. One difference between the Principles of Corporate Governance and Guidelines may be in the fact that the OECD is dealing with Multinational companies. This is one difference from the *Principles*, which are intended to guide national corporate governance implementation. Perhaps the *Guidelines* were drafted without much hope because MNEs have so much power that so even the OECD are reluctant to lecture them. Alternatively they know that there is no legal entity known as a ‘multinational company’ and therefore it is extremely complex to regulate (even in a soft law way) all of the subsidiaries⁹³ and the parent company⁹⁴ in a MNE. Yet there is an evident reluctance to see the sustainable development and environmental issues as a ‘corporate governance’ concern; this is particularly pertinent for the later argument about growth and the sustainability of the planet, but as well for all ethical problems besetting all companies.⁹⁵ The *Principles of Corporate Governance* states that the board of a company to has responsibility to “promote transparent and efficient markets, [and] be consistent with the rule of law”⁹⁶ This is in

⁹¹ Muchlinski, P, *Multinational Enterprises*, OUP, 1995, p579.

⁹² Preface, para 10.

⁹³ This is using a simplistic model of Multinational companies, there are a multiplicity of patterns of arrangements, including franchises, cross-shareholder arrangements, joint ventures etc, see Eroglu, *Multinational Enterprises and Tort Liabilities*, Edward Elgar, 2008, Weitzenboeck, Emily M, *A Legal Framework for Emerging Business Models: Dynamic Networks as Collaborative Contracts*, Edward Elgar, 2012.

⁹⁴ Dine, Janet, “Jurisdictional Arbitrage by Multinational Companies: a national law solution”, *Journal of Human Rights and the Environment*, Vol 3, No. March 2012, pp. 44-44-69, Zerk, *Multinational and Corporate Social Responsibility*, Cambridge University Press, 2006, Muchlinski, P, *Multinational Enterprises and the Law*, Blackwell, 2007.

⁹⁵ Helm Dieter and Hepburn, Cameron, (eds) *The Economics and Politics of Climate Change*, Oxford University Press, 2009, Meadows, Randers, Meadows, *Limith to Growth*, Earthscan, London, 2012, Sandel, Michael, *What Money Can’t Buy: The Moral Limits of Markets*, Allen Lane, 2012

⁹⁶ OECD Principle, 1, page 17.

contrast to “Enterprises should, *within the framework of laws*, regulations and administrative practices in the countries in which they operate, and in consideration of relevant international agreements, principles, objectives and standards, take due account of the need to protect the environment, public health and safety, and generally to conduct their activities in a manner contributing to the wider goal of sustainable development”⁹⁷ Despite the fact that both documents urge the setting up of systems to monitor environmental performance, it remains clear that the governance model requires adherence to *the rule of law*, whereas the *Guidelines* exhort adherence to *the wider principle of ‘sustainable development’*. The only paragraphs in the *Principles* which have a wider reach than proper compliance with law appear in the Disclosure and Transparency section⁹⁸. On the basis that “Disclosure . . . helps improve public understanding of the structure and activities of enterprises, corporate policies and performance with respect to environmental and ethical standards, and companies’ relationships with the communities in which they operate”, companies are urged to “disclose policies relating to business ethics, the environment and other public policy commitments” and “risks relating to environmental activities”. However, “Disclosure requirements are not expected to place unreasonable administrative cost burdens on enterprises. Nor are companies expected to disclose information that may endanger their competitive position unless disclosure is necessary to fully inform the investment decision and to avoid misleading the investor”. So far as environmental damage is concerned, only problems that will affect the decisions of *investors* are material, informing the consumer is not necessary where a competitive disadvantage may be feared. This disclosure regime will only work to the benefit of the environment if we assume that all investors have an ethical approach. Thus a statement that ‘mahogany trees are being felled at a significant rate and turned into garden furniture netting a huge profit for investors will be unlikely to deter non-ethical investors whereas the other side of the story ‘we are chopping down ancient forests and creating a desert’ could be withheld on the basis that it is not material for investors and it would put the company at a competitive disadvantage.’ The *Guidelines* are much more positive in the environmental field requiring the maintenance of systems of environmental management, consultation with local communities, adopt a precautionary principle and prepare environmental impact reports.

There are several other problems with the approaches in the *Principles* and *Guidelines*. Apart from their non-binding nature⁹⁹ and the controversy over the status of corporations in international law (addressed above), it is also problematic that the *Guidelines* represent a form of ‘outside the company exhortation’ and it will be unlikely to be effective unless mechanisms to achieve sustainable development can become part of the internal governance systems of companies rather than outside encouragement. A third, and most fundamental problem is that it will not be possible to enlist company support for the wider meaning of ‘sustainable development’ until the underlying social understanding of the purpose companies serves changes fundamentally so that particularly if ‘sustainable development’ retains its original ambience which included a significant redistributive agenda.¹⁰⁰ The principal aim of MNEs is to maximise shareholder profit. It is for this reason that the mahogany statement may be regarded as acceptable disclosure to investors. Further, since the vast majority of the shareholders of MNEs live in the developed world the repatriation of

⁹⁷ OECD Guideline VI

⁹⁸ Part V

⁹⁹ See Zerk, *Multinationals and Corporate Social Responsibility*, CUP, 2006.

¹⁰⁰ Brundtland, H., *Our Common Future*, Oxford University Press, 1987.

profits made in environmentally damaging ways represents a regressive redistribution of wealth which is the precise opposite of the aim of ‘sustainable development’.

Before leaving the debate about corporate governance and the World Bank’s Template which was based on the revised OECD Principles of Corporate Governance 2004 it is important to remember that the template was “designed for use as the diagnostic tool for assessing the strengths and weaknesses of the corporate governance framework in a particular country”¹⁰¹ some small points which should be noted: In Question “378 “Do board members have to act in good faith and in the interest of the company” which is a bland assumption that everyone knows what the interest of the company is and which is a key question for the rest of this book. We know that there is a major debate about the inequality of directors’ remuneration and other less well paid employees but the *Template* says nothing about ordinary employees, nothing about the wages or conditions of the median worker or the proportional wage rates in the company. Again this is of great consequence in our quest to understand the difference corporate governance systems. What the *Template* confirms that the management is more powerful than other stakeholders. In the title section about remuneration the *Template* says “Aligning key executive and board remuneration with the longer term interests of the company and its shareholders. . . . C. Is board remuneration *high enough*¹⁰² to ensure that board members devote sufficient time to their duties?”¹⁰³ This suggests that the only problem about remuneration is whether the pay should be high enough, although Stiglitz argues that corporate governance as practiced by the neo-liberal institutions are part of the rise of inequality.¹⁰⁴

The assumptions in the World Bank Corporate Governance project are an insidious way of controlling states’ culture into a global corporate governance system for the convenience for the multinational companies, including the multinational banks and their subsidiaries. The neo-liberal corporate governance paradigm has not yet tipped into a slave trade mentality but history shows that terrible suffering can be perpetrated by a free-trade approach. *Laissez faire* economics led to the Atlantic Slave¹⁰⁵ trade probably the worst example of the Faustian Bargain where England was enriched on back of terrible suffering: “Sugar and tobacco production . . . developed hand-in hand with coerced and degraded labor: grasping for wealth, profit-maximising English planters relentlessly sought overseas markets, ruthlessly exploited fellow humans, accumulated narrowly concentrated power, and resonated very little to liberal ideas and higher values.”¹⁰⁶ Corporate Governance matters because it is a

¹⁰¹ World Bank *Template*, 2007, introduction.

¹⁰² My italics.

¹⁰³ ¹⁰³ http://www.worldbank.org/ifa/CG_template.pdf, accessed on 20/8/2012, my italics.

¹⁰⁴ . Stiglitz, *The Price of Inequality*, Allen Lane, 2012, page 66.

¹⁰⁵ Thomas, Hugh, *The Slave Trade*, Picador, Phoenix, 2006.

¹⁰⁶ . Nash G, “Forward” in R. Dunn *Sugar and Slaves: The Rise of the Planter Class in the English West Indies, 1624-1713* University of North Carolina Press, 1972 and 2000.

fundamental building block of the governance of commerce and therefore the economy of states and eventually the international economy. If companies are run with no compassion, the international economy will implode because of the endemic inequality which is the legacy of neo-liberal policies.

Contract, Freedom, Inequality, Democracy and Regulations.

The neo-liberal paradigm is a contractual based system. In a market economy contract is a crucial tool, however there are some fundamental problems in a *free* contractual market. A market economy is based on the theory that each individual has freedom to trade and this leads to each person getting their needs and desires satisfied. An economy which is mostly arranged on a contractual design means that there will be inevitably people who are disadvantaged. Where this happens contract can be a malign construct and eventually there will be a paradox, people will be limited in their choices although the whole idea of a contractual model economy was to enhance freedom. Where this happens in grossly unequal societies this is also a danger for democracy. If individuals are so poor that they are fighting to get enough food or water democracy will not be their first priority, nor can they access information or debate the political issues in the nation¹⁰⁷.

While at first sight an agreement between two individuals to buy and sell might seem a politically neutral transaction and therefore politically uncontroversial, as soon as any disparity of bargaining power is taken into consideration it becomes clear that the arrangement will tend to benefit the party who started in the more powerful position. A simple example to illustrating the way that inequality can quickly exacerbate divisions between people is the following¹⁰⁸: On a cold day I once had half an hour to kill before meeting my daughters from school. I went to buy a minor electrical item in a large electrical superstore. As I had some time I read (for the first time ever) the small print of terms and conditions of the sale, and found a term which I considered to be outrageous. I presented the item to the young person at the till announcing that I would like to buy the item but mentioning that I had crossed out this particular term as I didn't accept it. This caused a delightful chaos. Of course, the person at the till couldn't accept the changed bargain, so he called the supervisor, who called the store manager, who called the area manager. At this point, I ran out of time and left without the item. What the interlude illustrates is that large companies are used to dictating the terms on which they will deal. Such a contract is very far from being a contract between equals. Only if safeguards (such as unfair contract terms legislation) are enacted can the equation be rebalanced. Teubner illustrates the notion of contractual unfairness in a consumer marketplace as follows: 'A contractual term is unfair if "contrary to the requirement of good faith it causes a significant imbalance in the parties'

¹⁰⁷ Shue, Henry *Basic Rights*, Princeton University Press, 1996.

¹⁰⁸ Dine Janet, Inaugural Lecture at Queen Mary College, June 15th 2008.

right and obligation arising under the contract, to the detriment of the consumer”¹⁰⁹. Of course, this leaves unexplained the intractable question of which imbalances are ‘fair’ and what, therefore, what is meant by ‘good faith’. Teubner has pointed up some of these, in his work in transplanting laws between countries. Teubner argues that transplanting laws into a different jurisdiction is usually disastrous unless the country philosophic attuned. He uses contractual concepts to illustrate his concepts of fairness particularly Unfair Terms Contracts legislation. He illustrates the way that the UK courts rejected the requirement of good faith saying “The British courts have energetically rejected this doctrine on several occasions treating it like a contagious disease of alien origin and he cites *Walford v Miles*¹¹⁰: where the judge said that god faith is “inherently repugnant to the adversarial position of the parties’¹¹¹. For him this shows that the judicial system in the UK is imbued with contractual cultural connotations. The German understanding of good faith is more generous and inclusive involving the whole of society, not just the parties. Similarly company governance in Germany tends to follow a communitarian model. Arrangements for economic enterprises were profoundly different within continental Europe, but when the UK joined the EEC the existing divisions were exacerbated. German capitalism, for example, has a philosophical concept of ‘good faith’ which is the reverse of the UK-contractual paradigm. Teubner argues that arrangements in Rhineland capitalism are predicated on trust between all of the individuals in the company, its suppliers and their financial backers: ‘Economic action is closely coordinated by business association and by informal business network . . . These regimes give considerable autonomy to employees within the hierarchy of the organisation and to suppliers and deliverers within long-term cooperative networks. This opens opportunities for production prone to long-term cooperation, but creates simultaneously considerable risks that are typical for high autonomy and high trust relations.’¹¹² Transition countries are particularly prone to legislate using ‘experts’ from other countries and great care is needed to align the fundamental philosophy of the state including constitution, judicial system and commercial law it will be dysfunctional.¹¹³

¹⁰⁹ Teubner, Gunther, Vol 61 MLR, 1998 page 11.

¹¹⁰ Teubner, Vol 61 MLR, 1998 page 25..

¹¹² Teubner, Vol 61 MLR, 1998 page 25..

¹¹³ Dine, j, Koutsias, M., and Blecher, M., *Company Law in the New Europe: Acquis. Comparative Methodology Law*, Edward Elgar, 2007.

Economic Contractualism, and the rise of the Multinationals

Later we will consider in detail the corporate models which are found in America, Germany and the UK however the most important and influential companies in the western world use a contractual model. This means that always trade bargains are asymmetrical because of the imbalance between individuals' bargaining position.¹¹⁴ This is the well understood difference between the Pareto theory and the Kaldor-Hicks notion of efficiency. Pareto efficiency requires that someone gains and no one loses in a contract. In contrast, the Kaldor-Hicks test accepts as efficient 'a policy which results in sufficient benefits for those who gains that *potentially* they can compensate fully all the losers and still remain better off.¹¹⁵ Ogus explains this very simply and tellingly showing the difference between the tests using an example "Bill agrees to sell a car to Ben for £5,000. In normal circumstances it is appropriate to infer that Bill values the car at less than £5,500 (say £4,500) and Ben values it at more than £5,000. (say £5,500). If the contract is performed, both parties will gain £500 and therefore there is a gain to society-the car has moved to a more valuable use in the hand of Ben . . . this is said to be an "allocatively efficiently: consequence"¹¹⁶. Everyone is a gainer, this is an illustration of the Pareto efficiency test. This win-win situation is a Utopian vision and extremely rare because of the number of disadvantages that can be envisaged. The most obvious ones are power or money, therefore bargains are usually rigged because of imbalance between the parties. Because of the rarity of Pareto bargains a different test was designed, the Kaldor-Hicks principle, where in an economy the good bargains and bad bargains are averaged.¹¹⁷ Unfortunately in the Kaldor-Hicks there is no reason why the gainer should compensate the loser and therefore in a contract where the loser is already disadvantaged he will probably become further deprived. This is also one reason why there is a more and more unequal world now

There is a sliding scale of contractual freedom in Western economies which allows some commercial laws to be enacted without proper consideration of the risk borne by the disadvantaged. Because of the power of MNCs they can dictate terms, to employees and

¹¹⁴ The fictive nature of companies are also crucial: "Denial of a separate personality to the entity form by the human group of actors is a necessary foundation for the application of market theories, since the underlying assumption is the creation of maximum efficiency by individual market players bargaining with full information. Tacking the view that free markets are the most effective wealth creation system neo-classical economists including Coase have analysed companies as a method of reducing the costs of a complex market consisting of a series of bargains among parties." Dine, "Jurisdictional Arbitrage by Multinational Companies: a national law solution", *Journal of Human Rights and the Environment*, Vol 3, No. March 2012, pp. 44-44-69,

¹¹⁵ . Greenfield, K, 'From Rights to Regulation' in Patfield, F, (ed), *Perspectives on Company Law: 2*, Kuwer, London 1997, page 10.

¹¹⁶ Ogus A., Regulation A, : *Legal Form and Economic Theory*, Clarendon Press, Oxford 1994 page 24

¹¹⁷ Ogus, A., *Regulation*, page 24.

suppliers but also to governments. A contractual design of a free market is appears to be good for individual freedom but it is a chimera; freedom is disguised as a form of neutrality and equality:

“Every stable social system possesses an order of power and wealth, but unlike historically prior distributive schemes, the market order avoids the imposition of a detailed pattern. Instead of a structure of rank and privilege fixing entitlements to wealth and power, the distributive mechanism of the market allocates resources to those persons able and willing to pay the highest price for them . . . The market order avows blindness to claims of privilege or force, so it recognises no claims of an inherent right to govern or to possess superior wealth . . . The market order lets fly the centrifugal forces of radical individualism, permitting philosophers to celebrate the relative fluidity of its distributive outcome and to legitimate it by appeals to the impervious mask of market forces. No other order so successfully disguises the fact that it constitutes an order at all.”¹¹⁸ The same argument works in exactly the same way at an international political level. An agreement between states with equal bargaining power may be considered to be politically neutral, when they are of disparate power the ‘contract’ is of profound political importance. In this respect it is significant that the first quasi-judicial enforcement mechanisms at international level have been designed and operate to enforce international commercial law and clearly favour richer nations with more diverse economies. The neo-liberal design which the world is imbued is an aggressive sort of capitalism but it is not completely new. It has an uncanny resemblance to the way in which the English colonized North America. “The English could congratulate themselves on the honourable way they were populating North America. They could see the Indians growing poorer but they did not conceive that they were the agents of the Indian’s impoverishment. They were not taking the Indian’s land by force of arms, after all. They were buying it on the open market.”¹¹⁹ There were transactions called “Treaties” . . . but of course they weren’t genuine contracts, because the Indians didn’t *consent* to sell their land. Indians had different conceptions of property than European settlers had, so they couldn’t have understood what the settlers meant by a sale. The Indians were really conquered by force . . . but Americans and their British colonial predecessors papered over their conquest with these documents¹²⁰ to make the process look proper and legal.¹²¹ What was happening for the Indians was that they completely missed the importance of a key concept. The Indians had a concept of property which land was community- owned, therefore the individual-contract idea was entirely

¹¹⁸.Collins, H, *The Law of Contract* (1986), cited in . Campbell D, “reflexivity and Welfarism in the Modern Law of Contract” (2000) Oxford Journal of Legal Studies 477.

¹¹⁹ . Banner, S, *How the Indians Lost their Land*, Harvard University Press, Cambridge, Mass, 2005

¹²⁰ Crashaw William, “A Christian may take nothing from a Heathen against his will, but in faire and lawfull bargaine,”¹²⁰

¹²¹ Banner, *Indians*, P1.

foreign for them.¹²² When we consider corporate governance in detail for each jurisdiction we will see how decisive the language and concepts are. Perhaps this can be best illustrated by the differences of the Anglo-American contractual model which accentuate the fictive nature of companies, born from negotiation by individuals agreeing a contract as against an organic understanding of company as a living entity which is prevalent in German jurisprudence.¹²³ This latter theory is more conducive for corporate social responsibility practitioners and academics who promote stakeholder models.¹²⁴ However on the global stage, the contractual model of companies has been the way that Multinational Companies have enhanced their prestige and power with devastating consequences¹²⁵. The argument starts with single companies using a contractual model and turns into the giant MNEs that we are so familiar now. The rise of the mega companies was engineered by the neo-liberal paradigm using contract, free market philosophy and deregulation. On the international stage states were often pressured by the neo-liberal institutions including the World Bank, the IMF and the WTO to believe that growth and development was crucial for all nations including the developed countries. This is now becoming challenged by a growing number of thinkers who believe that continuing the pattern of unlimited growth is damaging the earth and simultaneously bad for human health, mental and physical.¹²⁶ These authors cite different reasons for their beliefs some use utilitarian theories others cite spiritual reasons. However if they are right it is will be important to incorporate these ideas in corporate governance and

¹²² See also the tensions between collectivism and individualism in the Soviet system, . Hill, J, “Corporate Corporate Governance and Russia-Coming Full Circle”, LAW, LEGAL CULTURE AND POLITICS IN THE TWENTY FIRST CENTURY - ESSAYS IN HONOUR OF ERH-SOON TAY, Alice, , p. 153, Doeker-Mach & Ziegert, eds., Franz Steiner Verlag 2004

¹²³ Keay, *The Corporate Objective*, 2011, pages 33-35 and see also Edward, V, *EC Company Law*, Oxford University Press, 1999, page 35,

¹²⁴ .Keay, *The Corporate Objective*, 2011, Chapter 3, Teubner, Gunter, “Enterprise Corporatism; New Industrial policy and the ‘essence of the Legal Person’” (1988) 36 *American Journal of Comparative Law* 130 and Worthington, “S, Shares and Shareholders: property, Power and Entitlement (Part 2) (2001) *The Company Lawer* 307., Dine, J, *Companies, International Trade and Human Rights*, CUP, 2005.

¹²⁵ Dine, J, “The Governance of Corporate Groups” CUP 2000, page 152, Seealso for example Larsson, T, *The Race to the Top; The Real Story of Globalisation* Cato Institute, Washington, 1999, Irwin, D, *Free Trade Under Fire*, Princeton University Press, New Jersey 2002, a slightly more balanced approach in Moore, M, *World Without Walls* Cambridge University Press, 2002, Glinavos, I, *Neoliberalism and the Law in Post Communism Transition*” Routledge 2010.

¹²⁶ Skideksky and , Skidelsky, *How Much is Enough?*. Allen Lay, 2012, Stigliz, J, *The Price of Inequality*, Allen Lay, 202012, Willkinson , Richard, and Pickett, Kate, *The Spirit Level*, Penguin, 2009, 20010,1 Sandel, Michael, *What Money Can't Buy*, Allen Lay, 2012, Green, Duncan, *From Poverty to Power*, Oxfam, 2008, J. Dine, *Companies, International Trade and Human Rights*, CUP,, 2005.

embed it in national jurisprudence. From the global perspective this is particularly difficult because of the international traditional understanding of sovereignty of states; Nations jealously guard their own interests even though their prerogatives are more and more compromised by globalisation and the power of the multinational companies¹²⁷. To construct a global corporate governance system which balances not only national stakeholders' interests but also governmental interests and global environmental issues is a true challenge¹²⁸ So far there is no possibility of agreement on such agreement. Absent any agreement national corporate governance might be improved to ameliorate inequality. The quirks and priorities of national corporate governance will be explained in Chapters 3-5. We will see that although the neo-liberal paradigm is very powerful, there are significant differences between national corporate governance systems.

Multinationals legal structures and Extraterritoriality.

It is odd that many corporate governance texts ignore groups of companies even though Multinational companies are becoming more powerful than some states and governments.¹²⁹ We have seen the intractable problems set by MNEs including the democratic deficient, environmental damage and the growing gap of inequality. We charted the strict jurisprudence in the UK and the USA which adheres to a stringent separation between shareholders and the company. In the case of *Salomon*¹³⁰ In the House of Lords, Lord MacNaughten stated: 'The company is at law a different person altogether from [those forming the company]: and, though it may be that after incorporation the business is precisely the same as it was before, and the same persons are managers, and the same hands receive the profits, the company is not in law the agent of the subscribers or trustee for them. Nor are the subscribers as members liable, in any shape or form, except to the extent and in the manner provided by the Act... If the view of the learned judge were sound, it would follow that no common law partnership could register as a company limited by shares without remaining subject to unlimited liability.' The idea is that the company is an entity separate from the people actually involved in it. This fictional 'legal person' owns the property of the business, owes the debt to business creditors and is in full position to become a party in legal relations;

¹²⁷ Beck, *Power in the Global Age*, Polity, 2005.

¹²⁸ However, designing a corporate governance system is challenging not only because of their power but also because of the fictive nature of multinational companies. In legal parlance TNCs are not recognised as an entity, they are not able to own property or to sue or sued. They are not legal persons, of course, sociology recognises as viable groups, part of society, but legally they are only linked companies either by shareholders or, more radically, by power (one company might be subordinate to another). This legal flexibility is one reason why they have allowed us to dominate the western hemisphere.

¹²⁹ See the beginning of the introduction of this book, but see Dine J *The Governance of Groups*, Cambridge University Press 2000, Andenas, Mads and Wooldrige, Frank, *European Comparative Company Law*, , Cambridge University, 2009,

¹³⁰ *Salomon v. Salomon* [1897] AC 22

it can sue and be sued on its own, it can become a party to a contract and very significantly it retains its identity and business despite radical changes in the composition, number or identity of its founders and at times membership. This translates into the international context allowing MMNEs to play 'jurisdiction arbitrage'¹³¹. Frequently, in the case of environmental hazards, a parent company can hive out risky or dirty business abroad. Problematically, if there is a violation of the environment the subsidiary company will generally not be sued, either because the venture is in a state which is politically unstable and/or lacking in effective environmental regulation or enforcement practices, or because the subsidiary can be starved of finance by the parent and placed in danger of insolvency. Meanwhile, suing the parent company is problematic because each company in the MNC group is constructed as being completely separate. Each jurisdiction, moreover, has a limited jurisdictional reach, whilst, in effect, each company in the MNC group is insulated by the operation of the 'corporate veil' isolating the companies making up the group. In this sense, the MNC makes a particularly complex target for the imposition of liability: there is no single MNC 'entity', as such. Constructing a form of 'enterprise liability', however, would potentially mean that the whole MNC enterprise could be sued simultaneously, making it simpler to force the directors of each company to respect standards of environmental probity and any relevant fiduciary duties. The growth of MNCs has been possible precisely because most legal systems regard one company holding shares in another in exactly the same way as if the company were a human individual shareholder.¹³² Most legal systems take no account of the reality of the accumulation of power represented by a large number of companies related by interlocking shareholdings, despite the fact that many companies are organised in a 'group' structure wherein control is exercised over a number of subsidiaries through shares held by a 'parent' company. While the simplest case is a hierarchy with 100% shareholding by a parent company there are numerous other ways of creating effective control of one company over others through a range of share structures and other contractual devices like franchises and joint ventures.¹³³

The fictive nature of companies gains a new level of complexity, therefore, in the case of MNCs, and the fundamental 'non-existence' of the MNC as an 'entity' is arguably intimately related to the problem presented by the extraterritoriality of national jurisdiction. Each nation-state has equal sovereign power to regulate the territory that it owns, and enacts its

¹³¹ Dine, J, "Jurisdictional Arbitrage by Multinational Companies: a national law solution", *Journal of Human Rights and the Environment*, Vol 3, No. March 2012, pp. 44-44-69

¹³² Dine., *The Governance of Corporate Groups*, CUP 2001, Blumberg, P., "The American law of Corporate group" in McCahery.J., , S.Picciotto and Scott ,C., (eds.), *Corporate Control and Accountability* , Clarendon, Oxford, 1993.

¹³³ Weitzenboeck., Emily., , *A Legal Framework for Emerging Business Models.*, Edward Elgar, 2012.

own laws. Companies are a legal *fiction*¹³⁴ invented by national law. Each state possesses the power (and usually the exclusive power) to regulate the company and to enforce its liabilities. However, as has been suggested already, MNCs do not exist as an ‘entity’ defined or recognised by law. MNCs are, rather, complex structures made up of individual companies in a variety of interrelationships.¹³⁵ While globalisation means that the world appears to be a smaller place, and while goods and people can move freely across borders, companies remain legally tied to the country where they are formed. The operation of equal sovereign power, however, normally means that regulations made in one jurisdiction, in the normal course of events, cannot have any impact on corporate liability in another. This is the problem of extraterritoriality. The fact that MNCs are series of companies formed in different national legal systems and tied together in various legal ways, either by holding shares in each other or by various legally binding agreements between them, presents genuine complexity. This complexity, moreover, is exploited by MNCs. There are numerous cases, for example, of parent companies exporting dirty and dangerous business to poor countries where regulations are minimal or not enforced; or of paying exploitatively low wages; and/or ignoring the environmental effects of corporate operations.¹³⁶ Poorer countries, meanwhile, are often desperate for any foreign investment – and thus rendered especially vulnerable to such practices.

The practical implications of MNC complexity can be devastating. Suppose, for example, that damage is done to the health of employees of a company. The employees will find it difficult or impossible to claim against the local operator in some countries, especially

¹³⁴Zerk, Jennifer., *Multinationals and Corporate Social Responsibility*, CUP, 2006, Muchlinski, Peter., *Multinational Enterprises and the Law*, (2nd ed) OUP, 2007, Dine., , *Companies, International Law and Human Rights*, CUP, 2005

¹³⁵ See the US Third Restatement, ALI ‘restatement of the Law, Third, Foreign Relations’ para 213; “For purposes of international law, a corporation has the nationality of the state under the law of which the corporation is organised. And ‘Multinational Corporations’: The Multinational enterprise or corporation . . . is an established feature of international economic life, but it has not yet achieved special status in international law or in national legal system. A multinational corporation generally consisted of group of corporations, each established under the law of some state, linked by common managerial and financial control and pursuing integrated policies, see also Zerk, *Multinational and CSR*, page 149-150.

¹³⁶ .Just some of them are Simms, Andrew, and Boyle, David, *Eminent Corporations*, Constable & Robinson Ltd, 2010, Monbiot, George, *Captive State: The Corporate Takeover of Britain*, , Macmillan, 2000, Korten, D., *When Corporations Rule the World*, , Kumarian 1995, Klein, N., *No Logo*, Picador 1999, Klein, N., *Fences and Windows*, Picador 2002, Hertz., .N., *The Silent Takeover*, Heinemann, 2001, Chomsky.M., *Profit over People*, Seven Stories Press, New York 1999, Palast., G., *The Best Democracy Money Can buy* Pluto 2002, Ehrenreich .B., *Nickel and Dimed* Granta, London 2002, Schlosser,E., *Fast Food Nation* Penguin, London 2002 M Toynbee., *Hard Work* Bloomsbury London 2003,, Hutton., *The World We’re In* Little Brown, London 2002, Chossudovsky., *The Globalisation of Poverty*, Pluto, Halifax, Nova Scotia, 1998, Harrison., *Inside the Third World*, (3rd ed) Penguin, Harmondsworth 1993, Hertzgaard., *Earth Odyssey*, Abacus, London 1999, Karliner., *The Corporate Planet*, Sierra Club, San Francisco 1997.

if the legal system is structured to favour the MNC because of the need to attract foreign investment and/or if the legal system is corrupt or dysfunctional. Moreover, the layers of the corporate veil mean that the employees will find it impossible to claim against the foreign 'parent' company, because it is a separate company, structured according to the laws of a different jurisdiction, and not *legally* responsible for the acts of other companies in the MNC group even if they are very closely tied together through share-owning or by contractual arrangements. Drafting a law which encapsulates the complex range of legal structures of MNCs,¹³⁷ presents an extremely intricate challenge, for as we can see, each MNC is a complex of companies founded and governed by the commercial laws of different nation-states. The companies can be connected in a multitude of ways, by contract, by franchising agreements and by cross-shareholding, yet, despite this density of interconnection, there is no overall legal regulation of the whole commercial enterprise.

Only in very exceptional cases will the courts in rich countries break with general practice and 'lift the veil', that is, look to the reality of the situation.¹³⁸ Perhaps the most egregious example of the problem of extraterritoriality was the English case, *Adams v Cape Industries*.¹³⁹ Several hundred employees of the corporate group headed by Cape Industries had been awarded damages for injuries incurred as a result of exposure to asbestos dust in the course of their employment. Many of them were dying an unpleasant and lingering death. The damages had been awarded by a court in Texas, but Cape Industries had no assets in Texas, so the claimants could get no monetary compensation there. The claimants sought to enforce the claims in England, where Cape had its head office and considerable assets. The English Court of Appeal held that the awards could not be enforced in England against Cape even though one of the defendants was a subsidiary of Cape's and despite the fact that the group had been restructured in order to avoid liability. The purpose of restructuring, moreover, was blatant: The US subsidiary (which had been responsible for marketing in the US (North American Asbestos Corporation (NAAC)) was put into liquidation and ceased to exist. Instead, two new companies were formed: a company in Liechtenstein whose shares were held by a subsidiary of Cape, and an Illinois company ((Continental Productions Corporation) (CPC)) whose shares were held by the ex-president of NAAC. The two companies were also put in charge of US marketing. As a result of this, while there remained no *legal* link between Cape and CPC because Cape no longer held any shares, the reality was that the ex-president (who held all the shares) remained loyal to Cape's interests and controlled CPC. Additionally, in the case of CPC, a new legal link was introduced to add to the chain which connected Cape to its marketing operation. These moves were clearly and

¹³⁷ See Zerk, *Multinationals and Corporate Social Responsibility* (CUP: Cambridge 2006) at 51; M Weitzenboeck, *Between Contract and Partnership: Dynamic Networks as Collaborative Contracts and More* (PhD Thesis, Oslo University, April 2010).

¹³⁸ Zerk, *Multinationals and Corporate Social Responsibility*, CUP, 2006, see page 55 to illustrate some examples of lifting veil legislation. Interestingly she uses the UK Company Law 1985, section 751, to show that parents might be responsible for subsidiaries if the parent was a 'shadow director' now superseded by the Company Law 2006.

¹³⁹ 1990 BCLC 479.

openly intended to avoid liability for the outstanding claims for asbestosis injury which Cape knew were in the pipeline. Yet, Slade J reasoned that:

Our law, for better or worse, recognises the creation of subsidiary companies, which, though in one sense the creation of their parent companies, will nevertheless under the general law fall to be treated as separate legal entities with all the rights and liabilities which would normally attach to separate legal entities ... We do not accept as a matter of law that the court is entitled to lift the corporate veil as against a defendant company which is the member of a corporate group merely because the corporate structure has been used so as to ensure that the legal liability (if any) in respect of particular future activities of the group ... will fall on another member of the group rather than the defendant company. Whether or not this is desirable, the right to use a corporate structure in this way is inherent in our law.

And

If a company chooses to arrange the affairs of its group in such a way that the business carried on in a particular foreign country is the business of the subsidiary and not its own, it is, in our judgment, entitled to do so. Neither in this class of case nor in any other class of case is it open to this court to disregard the principle of *Salomon v Salomon* [1897] AC 22 merely because it considers it just so to do.¹⁴⁰

Such a legal outcome is commonplace throughout the world. This means that companies can export potentially liability-attracting activities away from the rich world to poverty stricken areas where *any* sort of employment, including scavenging from rubbish tips, is welcome and there are fewer, or no, inconvenient checks on health and safety, environmental or labour standards. The fact that in theory the subsidiary company in the poor country could be held legally answerable there is, as we have seen, no comfort. Quite apart from the possibility of corruption or dysfunction in the relevant national legal system, two further difficulties arise: First, the parent company can simply cause its creature in the poor country to disappear by instructing it to liquidate and if necessary transfer any funds to the parent company leaving the employees with a blank space: they have no company to sue – it has just disappeared; Secondly, any regulatory controls are frequently bargained away, in any case, before the company agrees to set up a business. These realities mean that MNCs can play regulatory or jurisdictional arbitrage, seeking out the jurisdiction with the fewest protections in order to maximise profit. This is the well-known ‘race to the bottom’, encouraged and protected by commercial law, just as was the slave trade in earlier times.

¹⁴⁰ Recently there is crack in English jurisprudence where tort liabilities for parent companies’ responsibilities for subsidiaries and their employees using a ‘control’ test: see *Chandler v Cape Plc* [2012] EWCA 525 and see Chapter 5 considering the German Law on company groups.

There are some exceptions to the strict doctrine of national sovereignty, though rare (the MNC lobby keeps a tight rein on legislation).¹⁴¹ Perhaps the best instance of a law purporting to tighten MNC accountability is the Foreign Corrupt Practices Act (FCPA) in the US.¹⁴² However, this Act failed to deliver on the early promise of its preceding Bill. Zerk records that:

In relation to ‘foreign corrupt practices’, for example, an early proposal to apply legislation directly to foreign subsidiaries of US-owned countries was rejected because of concerns about ‘the inherent jurisdictional, enforcement and diplomatic difficulties raised by the inclusion of foreign subsidiaries of US companies in the direct prohibitions of the Bill. ... This is despite concerns that a failure to extend the law to foreign subsidiaries would create a ‘massive loophole through which millions of bribery dollars would continue to flow’. A form of parent-based regulation of foreign companies is used instead: US parent companies can themselves be held liable under the Foreign Corrupt Practices Act (FCPA) for the acts of foreign subsidiaries outside the USA where the US parent company has authorised or directed ‘corrupt payments’ to be made.¹⁴³

While the new Act is a significant step forward it fails to live up to the promise of its Bill because disgorgement is the normal remedy, meaning that individual victims will not normally benefit from the legislation.¹⁴⁴ This suggests that the profits of redress for corporate malfeasance will accrue to the state, not individual victims, leaving a huge blank space in which individual victims will have no redress, particularly in tort cases.

Enforcement, as already implied, is, in any case, extremely complex. The problems are multiple. Extraterritoriality is one problem, but there is genuine difficulty in finding approaches able effectively to hold MNC power accountable. Often, for example, reliance is placed, unsuccessfully, upon soft power.¹⁴⁵ In the field of corporate accountability, for example, there is a widespread commitment to voluntarism, reflected in certain codes or principles and in the discourse of ‘corporate social responsibility’ (CSR), which still offers little in the way of direct enforcement despite its potential future promise for generating more diffuse forms of corporate accountability.¹⁴⁶

¹⁴¹ Zerk, *Multinationals and CSR*, 2006, chapter 3.

¹⁴² 15 USC 78dd-1

¹⁴³ Zerk, *Multinationals and CSR*, 2006, page 108.

¹⁴⁴ Weiss, David C., *The Foreign Corrupt Practices Act, SEC Disgorgement of Profits, and the Evolving International Bribery Regime: Weighing Proportionality, Retribution, and Deterrence*. *Michigan Journal of International Law*, Vol. 30, p. 471, 2009. Available at SSRN: <http://ssrn.com/abstract=1319814>

¹⁴⁵ Charlemagne *The Economist* “If Obama's America can't make soft power work, what hope does Europe have?” Mar 11th 2010, 13:26

¹⁴⁶ Although I have revised my assessment of Corporate Social Responsibility as a “moral Deflection device” which I wrote this in “2005, *Companies, International Law and Human Rights*, CUP, 2007, (from Pogge’s concept), born from frustration, I now believe that the academic and NGO community has made significant

Zerk¹⁴⁷ has documented the range of methods used by society to address the most egregious violations of human rights by MNCs: methods deploying a huge variety of pressure points, including codes, norms, reports, boycotts and internet activism.¹⁴⁸ MNCs themselves, however, are becoming involved in the debate,¹⁴⁹ and opinion on the promise of such initiatives, including scholarly opinion, remains sharply divided. A genuine question concerns the continuing influence of the Anglo-American neo-liberal philosophy, with its rampant individualism and consumerism¹⁵⁰. As we have seen, the neo-liberal, Chicago economic model values individualism overall ethical principles and rests on rationality, efficiency and information. This theory posits that a person acting rationally will enter a bargain which will be to his or her benefit.¹⁵¹ The most aggressive version of this model posits that a rational person wants maximisation of her assets.¹⁵² The whole structure of Western society is predicated on this hegemonic value system¹⁵³ and all individuals are imbued with some version of the theory. Since companies are manmade they are not immune from the prevailing culture. Because of this ethical businesses and CSR initiatives are faced with a powerful contraindication. It is, in the light of this, unsurprising that Zerk argues that

it is still extremely difficult to tell how far the core ideals of the CSR communities have become embedded in corporate culture. There is still plenty of scepticism within ‘civil society’ about the level of commitment of multinationals to self-regulatory schemes and social and environmental reform in general. Some multinationals have

inroad on MNCs’ violations and possibly it will be possible to enact a hard law in an international law context but I think it will be a slow process and using national law could be another channel to use, see next section.

¹⁴⁷ See also for example de Jonge, Alice., *Transnational Corporations and International Law*, Edward Elgar, 2011, Bottomley, S., and Kinley, D., (eds), *Commercial Law and Human Rights*, Dartmouth, Aldershot, 2002, Woodroffe, J., “Regulating Multinational Corporations in a World of Nation States” in Addo, M., (ed) *Human Rights Standards and the Responsibility of Transnational Corporations* Kluwer, The Hague, 1999, Skolgy, S., and Gibney, M., “Transnational Human Rights Obligations” (2002) *Human Rights Quarterly* 781, See also *Dine Companies, International Law and Human Rights*, CUP, 2005 especially pages 3-10.

¹⁴⁸ Zerk, *Multinational and Corporate Social Responsibilities: Limitations and Opportunities in International Law*, CUP, 2006, especially pages 21 and 94-101

¹⁴⁹ Id especially at page 99.

¹⁵⁰ UN Development Progress, *Human Development Report 1996 Oxford University Press, New York 1994; Third World Network*, “A World in Social Crisis: Basic Facts on Poverty, Unemployment and Social Disintegration”, *Third World Resurgence* (No. 52). 1994.

¹⁵¹ Williamson. O.E., , “Contract Analysis: The Transaction Cos Approach” in Burrows, P., and Velanovski, C., (eds) *The Economic Approach to Law* Butterworth, London, 1981.

¹⁵² Ayres , I., and Braithwaite, L., , *Responsive Regulation* Oxford University Press, Oxford 1992, Page 23.

¹⁵³ Hares. D., An interview with Archbishop Rowan Williams, Guardian Weekend 9/7/11 2011 “no one can any longer regard the free market as a natural beneficent mechanism , and how more sophisticated financial instruments have made it even harder to spot when the market’s causing real hurt.”

seen their environmental initiatives dismissed as ‘greenwash’, while other have been accused of using CSR-related initiatives as a way of diverting attention away from bad press elsewhere or as a tactical concession to avoid stringent legislation at some later stage.¹⁵⁴

CSR seems even more limited when placed against the background of the operation of limited liability and the weakness of international legal enforcement mechanisms. (In international trade law, in fact, there are only World Trade Organisation (WTO) enforcement mechanisms, widely seen as being counterproductive for the strengthening of labour conditions and for the protection of the environment.¹⁵⁵) However, it may just be that the huge CSR effort to counter environmental transgressions by MNCs may be bearing some limited fruit, though the evidence remains difficult to assess. It has been suggested that CSR standards are slowly becoming part of a normal societal understanding, and that CSR norms are becoming harder, a sort of middle way between hard law and ‘voluntary’ law.¹⁵⁶ Braithwaite and Drahos, for example, argue that ‘when many different types of actors use many dialogic mechanisms of this sort, both impressive regime regime-building and impressive compliance have been repeatedly demonstrated’.¹⁵⁷ This kind of accountability is arguably what Ruggie means when he uses a ‘social licence’¹⁵⁸ concept for MNC accountability.¹⁵⁹ The search for effective accountability, particularly in the face of the challenges of extraterritoriality, however, goes on.¹⁶⁰ Ruggie’s final report,¹⁶¹ moreover,

¹⁵⁴ Zerk, *Multinationals and CSR*, pages 100-101.

¹⁵⁵ Revesz, Richard. L., , Sands, Philippe., and Stewart, Richard. B., (eds), *Environmental Law, the Economy and Sustainable Development*, CUP, 2000.

¹⁵⁶ John Braithwaite, J., and Drahos, Peter., *Global Business Regulation*, CUP, 2000

¹⁵⁷ *Id.*, page 32.

¹⁵⁸ Human Rights Council, *Report of the Special Representative of the Secretary-General on the issue of Human Rights and Transnational Corporations and other Business Enterprises: Guiding Principles on Business and Human Rights Implementing the UN “Protect, Respect and Remedy” Framework: 2011.*

¹⁵⁹ Zerk, *Multinationals and CSR*, 2006, page 95, CSR norms are usually bottom-up concepts. Slaughter has suggested that international law should be replicated in a similar form including ‘reordering [the] relative priority [of] sources of international order’. This will change the way that Multinationals are viewed, any reorganisation must start from a perception that they are crucial in an international context, A. Slaughter “A Liberal Theory of International Law”, *American Society of International Law Proceeding* 240, 2000.

¹⁶⁰ Zerk, *Multinationals and CSR*, 2006. *Rehearsing the many initiatives by NGOs and parliamentarians and other groups to get a grip with extraterritoriality issues, see pages 160-196.*

¹⁶¹ <http://www.business-humanrights.org/media/documents/ruggie/ruggie-guiding-principles-21-mar-2011.pdf>, accessed on 9th August 2011.

offers little to overcome the problem. His ‘three pillars’ (which mirror the ‘protect, respect and fulfil’ motif of human rights standards with ‘protect, respect, remedies’), and his focus on ‘operationalizing’ seem to produce an unsatisfying lack of effective sanctions or reparations.¹⁶² Paragraph 25 of his report says that ‘[a]s part of the duty to protect against business-related human rights abuses, States must take appropriate steps to ensure, through judicial, administrative, legislative or other appropriate means, that when such abuses occur within their territory and/or jurisdiction those affected have access to effective remedy,¹⁶³ while paragraph 26 details the principles of judicial mechanisms. None of this, however, appears to amount to detailed, robust standards for effective MNC accountability, and extraterritoriality remains a stubborn barrier. We have also noticed the disjunction of Corporate governance and Corporate Social responsibility and the synergies and disparities between the OECD Guidelines for Multinational Enterprises (the Guidelines) 2011¹⁶⁴ and Principles of Corporate Governance 2004¹⁶⁵

The relative failure to hold MNCs accountable remains troubling. There are two remaining alternative approaches that this analysis will now consider: the first is based on the concept of universal jurisdiction, and the second, more promising, based on the idea of building a network of national laws enshrining ‘enterprise’ liability for MNCs. The first alternative is embedding an international law rule which lays down a principle of universal jurisdiction. There is no prospect of this solution working ever or at least only in the long term. The ‘revival’ of the Alien Tort Claims Act 1789 as a way of challenging corporate abuses has been claimed as a ‘beacon of hope’ by human rights activists.¹⁶⁶ Unfortunately, even this beacon of hope has now been extinguished or at least significantly doused. In *Kiobel v Royal Dutch Petroleum*¹⁶⁷ the judges by a majority said that a company could not be a sole defendant in a claim in an ATCA suit. There is still litigation in the US Supreme Court but it likely that this avenue will be blocked.¹⁶⁸ However a different possibility could be opened if the German Law of Groups and the EU competition rules were to be extended by national legislation. (see Chapter 5) Here we next need to extend our parameters to consider the consequences of a contractual economic model by considering the consequences of inequality and the democratic deficit

¹⁶² Id

¹⁶³ Id, para 25.

¹⁶⁴ www.oecd.org/.../0,3746,en_2649_34889_2397532_1_1_1_1,00.ht..., accessed on 22/8/2012.

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<http://www.oecd.org/daf/corporateaffairs/corporategovernanceprinciples/oecdprinciplesofcorporategovernance.htm>, accessed on 22/8/2012

¹⁶⁶ Earthright June 29th 2004 Press release

¹⁶⁷ US second circuit Court, Judgment September 17th 2010, italics in original.

¹⁶⁸ <http://www.business-humanrights.org/Documents/SupremeCourtATCAReview>, accessed on 30/10/2012. The Supreme Court’s decision expected in the first of 2013.

Inequality

“The extent of global inequality is breathtaking. The income of the world’s 500 richest billionaires exceeds that of its poorest 416 million people.”¹⁶⁹ An increasing chorus of academic literature, evidence from NGOs (Non-Governmental Organisations), the World Bank (WB), the United Nations Development Programme (UNDP) shows that inequality is becoming worse and exacerbating a range of problems from health issues (especially mental health) to obesity, life expectancy and happiness.¹⁷⁰ The causes are extremely to pinpoint accurately but so far many believe that at least some of the blame points to the neo-liberal Washington Consensus and its programme of deregulating the market, privatising public services and cutting the State¹⁷¹. This in turn gives private companies, particularly the large Multinational companies more power because they have more financial resources and therefore more power than national governments. As early as 2000 the World Bank *World Development Reports* were uncompromising. Setting out the numbers trying to live on less than \$2 or \$1 dollar a day one report (2000-2001) notes that “This destitution persists even though human conditions have improved more in the past century than in the rest of history – global wealth, global connections and technological connections have never been greater. But the distribution of these gains is extraordinarily unequal . . . And the experience in different parts of the world has been very diverse. In East Asia the number of people living on less than \$1 a day fell from around 420 million to around 280 million between 1987 and 1998 – even after the setbacks of the financial crisis. Yet in Latin America, South Asia, and sub-Saharan Africa the numbers of poor people have been rising. And in the countries of Europe and Central Asia in transition to market economies, the number of people living on less than \$1 rose more than twentyfold.”¹⁷² And, as we have already seen, some scholars argue that these figures underestimate the problem.¹⁷³ Similar conclusions about growing inequality were reached by the International Labour Organisation in its 2004 report *A Fair Globalisation*¹⁷⁴; while recognising that globalisation has great potential for good “we also

¹⁶⁹ UNDP *Human Development report*, 2005 and 2006, http://econ.worldbank.org/external/default/main?pagePK=64165259&theSitePK=478060&piPK=64165421&menuPK=64166093&entityID=000112742_20050920110826, accessed 0m 25/10/2012.

¹⁷⁰ Wilkinson and Kate Pickett, *The Spirit Level*, Penguin, 2009, 2012, UNDP *Human Development Reports*, 2005-2011, Green, *From Poverty to Power*, Oxfam International, 2008, Stiglitz, *The Price of Inequality*, Allen lane, Penguin, 2012, Mount, Ferdinand *Mind the Gap*, Short books, 2004 and revised edition 2012.

¹⁷¹ Wilkinson and Pickett, *The Spirit Level*, Penguin, 2009, 2012, UNDP *Human Development Reports*, 2005-2011, Green, *From Poverty to Power*, Oxfam International, 2008, Stiglitz, *The Price of Inequality*, Allen lane, Penguin, 2012, Mount, *Mind the Gap*, Short books, 2004 and revised edition 2012.

¹⁷² World Bank *Development Report 2000-2001*, OUP 2001, p3, See also Hertz *Silent Takeover*, pp40-41.

¹⁷³ Reddy, S. and Pogge, T., “How not to Count the Poor” www.socialanalysis.org, accessed on 21/12, 2012.

¹⁷⁴ ILO, Geneva, 2004

see how far short we still are from reaching this potential. The current process of globalisation is generating unbalanced outcomes, both between and within countries. Wealth is being created but too many countries and people are not sharing in its benefits . . . Many of them live in the limbo of the informal economy without formal rights and in a swathe of poor countries that subsist precariously on the margins of the global economy. Even in economically successful countries some workers and communities have been adversely affected by globalization. Meanwhile the revolution in global communications heightens awareness of these disparities.”¹⁷⁵ “Transnational companies (TNCs) are the driving force behind globalisation. Through their production, trade and investment activities, they are integrating countries into a global market. Through their control over resources, access to markets, and development of new technologies, TNCs have the potential to generate enormous benefits for poverty reduction. However, that potential is being lost. The weakness of international rules, bad policies and weak governance in developing countries, and corporate practices which prioritise short-term profit over long-term human development are undermining the capacity of poor countries – and poor people – to benefit from international trade.”¹⁷⁶ The immense power of corporations is indicated by a comparison between the economic wealth generated by corporations, measured by sales, compared with a country's gross domestic product (GDP). On this basis "the combined revenues of just General Motors and Ford . . . exceed the combined GDP for all of sub-Saharan Africa"¹⁷⁷ and fifty-one of the largest one hundred economies are corporations.¹⁷⁸ Further, the number of transnational corporations jumped from 7,000 in 1970 to 40,000 in 1998, and they account for most of the world's trade. They also stand accused of creating the current trade rules by their influence on government. Drahos and Braithwaite note that US Trade representatives ask the large corporations what they want from a trade negotiation and then negotiate accordingly.¹⁷⁹ "These corporations and their 250,000 foreign affiliates account for most of the world's industrial capacity, technological knowledge and international financial transactions. They mine, refine and distribute most of the world's oil, gasoline, diesel and jet fuel. They build most of the world's oil, coal, gas, hydroelectric and nuclear power plants. They extract most of the world's minerals from the ground. They manufacture and sell most of the world's automobiles, airplanes, communications satellites, computers, home electronics, chemicals, medicines and biotechnology products. They harvest much of the world's wood and make most of its paper. They grow many of the world's agricultural crops, while processing and

¹⁷⁵ ILO *Fair Globalization*, *ibid*

¹⁷⁶ Oxfam Report *rigged Rules and Double Standards*, Oxfam 2002, p175.

¹⁷⁷ Karliner, J., *The Corporate Planet*, 5; Global 500: The World's Largest Corporations (*Fortune* 7th August 1995), The World Bank *World Development Report 2000-2001* (OUP, 2001).

¹⁷⁸ Anderson , S, and Cavanaugh, J, *The Rise of Global Corporate Power* (Washington DC, Institute for Policy Studies, 1996).

¹⁷⁹ Drahos, P, and . Braithwaite,J, *Global Business Regulation*, Cambridge University Press, 2000.

distributing much of its food. All told, the Transnationals hold 90% of all technology and product patents worldwide and are involved in 70% of world trade."¹⁸⁰

Anna Grear also charts the recent changes of globalisation, including the opening of electronic communications, transport links, influential brands, and scientific advances and realises that the picture is one of transformation because of the power of transnational corporations. The author believes that mega-banks are clearly crucial in the world economy and the financial crash of 2008 and continuing instability has been a central pillar of the problems, saying "that there are reasons to suspect that the current crisis is not so much a crisis *of* neoliberalism but a crisis *within* neoliberalism concerning the best way to retain and protect of its fundamental tenets, structures and institutions,"¹⁸¹

With other commentators¹⁸² she argues that the financial crisis has crystallised further a situation which is 'socialised' by a strategy in which the private risk of the owners of capital are underwritten by the state, the losses of corporations and banks are mitigated by ordinary tax-payer and are "left holding future debts that in effect, simply pass the impact of the crisis to ordinary citizens"¹⁸³ Originally Multinational companies made products but as Stiglitz has shown us the next wave of consolidation was by the financial sector led by the IMF and the World Bank. The first attack was in the developing countries, now the developed states fear the market and politician are only puppets.

The Financial Crisis 2007-Risk free banking, neo-liberal policies and national strategies

¹⁸⁰ Karliner *The Corporate Planet*, 5; UNCTAD *World Investment Report 1995: Transnational Corporations and Competitiveness* New York: United Nations Conference on Trade and Development, Division on Transnational Corporations and Investment 1995, pp xix-xx.

¹⁸¹ Grear, Anna, *Redirecting HR*, Palgrave, page 9.

¹⁸² Na-Joon Chang "We stop protecting the rich from market forces", *Guardian*, 25/10/2012: "Gore Vidal . . . famously quipped that the US economic system of ' free enterprise for the poor and socialism for the rich' and see Ha-Joon Chang, *23 Things They Don't Tell About Capitalism*, Penguin, Allan Lane, 2010.

¹⁸³ Grear, *Redirecting HR*, Palgrave, page p and see also U. Beck *Power in the Global Age*, Polity. 2005.

Till the 2007 financial crash it was a strange aspect of the ‘globalisation debate’ that multinational companies were in the forefront of the debate and that the biggest banks were able to escape scrutiny. Originally attention focused on companies which produce tangible items which end up with a consumer. Activists focused on the wage conditions of employees or the violation of human rights or the pollution of the environment. This meant that there was an extra veil of invisibility to the operations of giant banks. Even though by 2003 the total assets of the top five banks were estimated at US\$4807294 million¹⁸⁴ their activities have frequently been left off the globalisation agenda. This changed radically on 2007 when the financial crash came and the numbers look very different now.¹⁸⁵ However, there is not a rigorous global reinvention of financial regulations and the IMF certainly has not changed its structural adjustment programmes rather in Europe it is merely supported by other institutions like the European Central Bank and the European Commission (the Troika)¹⁸⁶ There is no doubt that the way in which the global financial architecture has managed financial crises in a number of recent crises (including the ongoing crisis in the Eurozone) has given rise to unprecedented opportunities for banks to make huge profits while running virtually no risks. This is, in part because of the response that the IMF has made to those crises. Underhill and Zhang see the rise of multinationals as a threat to domestic political legitimacy by weakening states’ authority over macroeconomics and social policy and by being significant in the formulation of national economic policy; “integration with global financial structures has strengthened the position of private market actors over public authority. Powerful private actors come to dominate the formulation of national economic policies which, in their attempts to extract benefits from global integration, tend increasingly to serve the interests of market agents.”¹⁸⁷ (see more in the next section of this Chapter)

However, the International Monetary fund has largely (rightly) been vilified for the conditionality policies which it pursues, demanding severe cutbacks in social services in return for its loans¹⁸⁸, rather than the financial policies which it has pursued. Recently, however, the financial policies behind its activities have been questioned as well as the effect that its structural adjustment policies and their successors have had on the poorest within creditor nations. Stiglitz writes

¹⁸⁴ figures issued by Bank of America and reported in The Guardian, October 28th 2003.

¹⁸⁵ <http://www.federalreserve.gov/econresdata/statisticsdata.htm>, accessed on 11th October 2012.

¹⁸⁶ http://www.ekathimerini.com/4dcgi/w_articles_ws2_1_11/10/2012_465595, accessed on 11th October 2012

¹⁸⁷. Underhill,G, and Zhang, , “Global Structures and political Imperatives; in search of normative underpinnings for international financial order in ,G. Underhill and Xiaoke Zhang *International Financial Governance under Stress: Global Structures versus National Imperatives* Cambridge University Press, 2003, p78

¹⁸⁸ See. Dine *Companies, International Trade and Human Rights*, CUP, chapter 3.

“The IMF is pursuing not just the objectives set out in its original mandate of enhancing global stability and ensuring that there are funds for countries facing a threat of recession to pursue expansionary policies. It is also pursuing the interests of the financial community . . . Simplistic free market ideology provided the curtain behind which the real business of the ‘new’ mandate could be transacted. The change in mandate and objectives, while it may have been quiet, was hardly subtle: from serving global *economic* interests to serving the interests of global *finance*.¹⁸⁹ Capital market liberalisation may not have contributed to global economic stability, but it did open up vast new markets for Wall Street.”¹⁹⁰ This reassessment of the IMF turns partly on the ‘bail-out’ policies it has pursued. The allegation is that loans to risky areas are encouraged and underpriced because it is known that the IMF will support the country’s currency when a crisis threatens (see below). Eichengreen and Ruhl describe the ‘moral hazard’ thus; “Investors, it is argued, have been able to escape the financial costs of crises through the extension of international rescue loans. These “bailouts” (as they are described by their critics) give governments the funds they require to pay off their creditors, who are then able to exit the country free of losses. Not being subject to the cost of crises, investors disregard the risks of lending, and the consequent lack of market discipline allows feckless governments to set themselves up for a painful fall.”¹⁹¹

The allegation that the IMF is in the service of international finance essentially flows from the insistence by the IMF on liberalisation, in particular capital account liberalisation. The intended result of this is to permit capital flows to take place freely across the world. However, while this may be good for the financial community, it is not necessarily good for developing countries. “the cocktail of free capital flows, floating exchange rates, domestic financial liberalisation in G3 countries, and unregulated innovations in financial instruments and institutions such as derivatives and hedge funds has dramatically increased financial instability after the collapse of the Gold- Dollar standard.”¹⁹² The instability is a result of a system of liberalisation based on neo-classical assumptions, including perfect information flows. “If one asks which of the neo-classical assumptions fail in a way that permits [financial] crises to develop, it is the information structure on the basis of which lending decisions are made. Rather than each investor deciding individually his or her expectations on the basis of their estimate of the fundamentals, investors make their decisions on the basis of what others are expected to do, resulting in herd behaviour”¹⁹³ This assessment is based on Keynes’ beauty contest analysis, referring to a game in the UK tabloid press in the 1930s in

¹⁸⁹ italics in original

¹⁹⁰ Stiglitz ,J, *Globalisation and its Discontents*, Allen Lane, London, 2002, p206-7.

¹⁹¹ Eichengreen,B, and . Ruhl,C, “The Bail-in Problem: Systematic goals, Ad Hoc Means” <http://emlab.berkeley.edu/users/eichengr/>

¹⁹² L.Taylor< L, and . Eatwell,J. *Global Finance at Risk* New York, The New Press, 2000, cited Oxfam *Global Finance*,, 26.

¹⁹³ . Williamson,J, “Costs an Benefits of Financial Globalisation” in Underhill and Zhang, *International Financial Governance*, p44

which readers were asked to assess from pictures which women would be judged as the most beautiful by the entire readership; “in other words, readers would not win by giving their own opinion about the women’s beauty, not even by assessing what others’ personal opinions would be, but by guessing what people would, on average, believe average opinion to be. In financial markets, a trader will not bid a price according to what he or she believes an asset’s fundamental value to be, but according to what he or she assesses average opinion to be about average opinion of the asset’s value. The beauty contest analogy helps understand why market participants tend to engage in ‘momentous trading’ (i.e. herd behaviour) and why market valuations are subject to sudden shifts in ‘market sentiment’.”¹⁹⁴

Underhill and Zhang point out that “more than seventy financial and monetary crises of different proportions and characteristics have occurred in both developed and developing countries over the past two decades.”¹⁹⁵ They see as “A common background to these developments . . . the intensifying process of global financial liberalisation and integration As financial crises have become more frequent and more severe over the past two decades, this has raised the question of whether the growing frequency and severity of crises correlate with the emergence of this liberal and transnational financial order.”¹⁹⁶

While domestic policies have a large part to play in countries’ financial crises, many studies now show that two other factors have great significance. One is the role of speculators and the second is “ ‘crony capitalism’ at the global level, in the form of IMF bailing out Wall Street.”¹⁹⁷ Opportunities for speculators increase every time markets are opened, as do opportunities for the most powerful multinational banks. The role of the ‘bail-out’ mechanism is discussed below. Following the Asian crisis of 1997-8 a flurry of reports sought to identify the root causes.¹⁹⁸ Story identifies two distinct interpretation; an internalist explanation which sought to blame the governments suffering the crises and an externalist argument focussed on the international financial markets.¹⁹⁹ It is important to be aware of the possibility of ‘explanatory nationalism’ leading the IFIs to the most convenient explanation,

¹⁹⁴ Oxfam *Global Finance*, 26.

¹⁹⁵ . Underhill and Zhang *International Financial Governance under Stress: Global Structures versus National Imperatives* Cambridge University Press, 2003, p1

¹⁹⁶ Underhill and Zhang *International Financial Governance*, p1.

¹⁹⁷ Oxfam *Global Finance*, 28.

¹⁹⁸ IMF *International Capital Markets* Washington DC, IMF 1998, *World Economic Outlook*, Washington, IMF, 1998; Group of 7 *Declaration of G-7 Finance Ministers and Central Bank Governors* G7 1998, www.imf.org/external/np/g7/103098dc.htm; Group of 22 *Report of the Working Group on International Financial Crises*, Washington, G-22, 1998; *Report of the Working Group on Transparency and Accountability*, Washington, G-22, 1998; United Nations Executive Committee on Economic and Social Affairs *Towards a New International Financial Architecture* Santiago, Economic Commission for Latin America and the Caribbean, 1999

¹⁹⁹ . Story,J, “Reform: What has been Written?” in Underhill and Zhang (eds) *International Financial Governance*, p27

exonerating them from blame. A classic proponent is Moore; “most of the responsibility for these [Asia 1997, Argentina 2002] collapses lies with domestic policy-makers, of course” despite, in the same paragraph admitting that the very magnitude of money flows create forces so great that “they are difficult for all but the most powerful nations to resist.”²⁰⁰

The ‘internalist’ explanation of the Asian crises sees the cause of the collapse “as lying in the close connections established within the states between politics and bank-centred financial systems. The states provided implicit guarantees to banks, encouraging the banks to lend to corporations with good political contacts. As capital controls were eased, foreign creditors lent to the banks and credit exploded despite multiple warning signals ahead of June 1997. Externally, the inflow of capital to the East Asian countries was stimulated by the near zero interest rates prevailing in a moribund Japan, and by continued investor pessimism about business prospects in Europe. Consumption and imports boomed, just as volume export growths plummeted. With China’s accelerated move into world markets, foreign investors switched their attention to opportunities on the mainland, so that east Asian balance of payments’ dependence on short-term capital flows increased. When the Thai ‘wake-up call’ came, alerted investors withdrew in haste from one currency after another.”²⁰¹

The externalist explanation focussed more sharply on the instability inherent in liberalisation followed by ‘herd behaviour’.²⁰²

Recent crises involve twin banking and financial crises.²⁰³ “They were initially attributed to poor financial regulation and supervision as well as poor monetary policy, thereby putting the blame back on national governments and their “crony capitalist” clientele. . . It is now recognised that third generation crises are more complex, and may also include multiple equilibria effects, originate from abroad due to contagion effects or involve “crony capitalism” at the global level, in the form of IMF bailing out Wall Street.”²⁰⁴ Analysing the East Asia crisis, Stiglitz writes; “in retrospect, it became clear that the IMF policies not only exacerbated the downturns but were partially responsible for the onset: excessively rapid financial and capital market liberalisation was probably the single most important cause of the crisis, though mistaken policies on the part of the countries themselves played a role as well.”²⁰⁵ The most significant of those policies is the liberalisation of capital flows. The Eurozone crisis has followed the same path as the developing countries, including the structural adjustments of government policies. The Greek bailout cost £23 billion the conditionality conditions were protracted and bitter with tough budget cuts. However “Despite the bailout, the ongoing fragility of the Greek economy was underlined by the latest

²⁰⁰ Moore *World without Walls*, p32.

²⁰¹ . Story, J, “reform”, p27.

²⁰² Soros, George, *The Crisis of Global Capitalism: Open Society Endangered* , New York, Public Affairs, 1998.

²⁰³ . Sharma, S, *The Asian Financial Crisis*, Manchester University Press, 2003

²⁰⁴ Oxfam, *Global Finance*, 28.

²⁰⁵ Stiglitz *Globalisation*, p91.

unemployment statistics, which showed the country's jobless rate jumped to a record 20.7pc in the fourth quarter of 2011. Young people have been worst affected, with almost four in ten people aged between 15 and 29 out of work, up from 28pc a year earlier. The Spanish economy is also struggling. House prices in the country fell by 11.2pc in the final three months of last year, compared with the same period a year earlier. It was the fastest pace of decline since 2007 when the National Statistical Institute's series began, and left prices around 22pc lower than their pre-crisis peak.”²⁰⁶

Loans from either the IMF or World Bank come, not only at a financial price but at the cost of agreement to ‘structural reforms’. While the IMF denies absolutely that it has any role in political matters many have argued the contrary case. Stiglitz puts the matter succinctly; “The IMF took rather an imperialistic view . . . since almost any structural issue could affect the overall performance of the economy, and hence the government’s budget or the trade deficit, it viewed almost everything as falling within its domain’ . There is now a significant democratic deficit in Europe. “The sheer reality of global corporate dominance has produced a situation in which human rights discourse struggles to retain critical distance from the human rights-colonising activities of formations of global capital . . . Quite simple, it is essential not to underestimate the influence of [Transnational Companies] TNCs in the current world order”²⁰⁷ Since the foundation of the human rights movement was the attempt to free people from the dominance of the state human rights discourse is struggling with the new dominance of TNCs which are supreme in world politics and economic influence.²⁰⁸ This tells some scholars that the Human Rights movements are being captured by international capital or at least complicit with it, particularly in making inequality worst.²⁰⁹

We will see some national corporate governance solutions in other Chapters which could lessen the impact of financial crisis by short-term strategies in companies including twin boards, employee participation and quotas of non-executive directors. Policy makers should study these solutions carefully and simultaneously make sure that these solutions will fit in the national psyche. The solutions will not be found only in corporate governance but also in tightening the ethical standards of lawyers and accountants.

²⁰⁶ Monaghan, Angela, *IMF gives formal approval for Greek Bailout*, Telegraph, 15th March 2012.

²⁰⁷ Grear, *Redirecting HR*, Palgrave, page 9.

²⁰⁸ . Beck *Power in the Global Age*, Cambridge: Polity Press, 2005, D. Korten *When Corporations Rule the World*, Kumarian Press, 1995, p3

²⁰⁹ . Douzinas, C, *Human Rights and Empire: The Political Philosophy of Cosmopolitanism*, Abingdon, Poutledge-Cavendish, 2007, . Evans,T, and . Ayers,A. J., “In the Service of Power; The Global political Economy of Citizenship and Human Rights” (2006) 10 *Citizenship Studies* 239..

Democratizing and De-Democratizing

Now we have seen how the neo-liberal theories of free markets, privatisation and a small state has been constructed, now we need to consider what are the implications for states, their governments, their populations and democracy: Beck argues “ We are witnessing one of the most important changes there has been in the history of power. Globalisation needs to be decoded as a creeping, post revolution, epochal transformation of the national and international state-dominated system governing the balance of power and the rules of power. A *meta-power game* is in progress in the relationship between global businesses and the state, a power struggle in which the balance of power and the rules of power governing the national and international systems of states are being radically changed and rewritten.”²¹⁰ Of course the new power in the game is the enormous companies especially the financial mega-banks, hedge funds and other speculators. It is not only the state that has been hollowed out, governments and political parties have also been affected. Beck argues that the neo-liberals have hijacked the arguments; “This is why national governments and political parties are so bland because the neo-liberal agenda are seduced by the neo-liberal concepts. “the global economic aims and principles of neo-liberalism breaks through national specificities and borders from the inside and accelerate processes of reform aimed at opening up the national to interdependencies”²¹¹ In particular such views lead to the undermining of the state as a responsible entity the purpose of which is to represent a collective morality and achieve a fair distribution of goods. It also inevitably points to the individual as providing the salvation for all, most importantly through the use of property transactions. The consumer as saviour is a direct descendant of these ideas. Globalisation is thus both driven by philosophies of open markets and fuelled by the consumerist, individual culture which operates at citizen level. Thus the citizen becomes a consumer with considerable impact on our understanding of democracy. If the state exists merely to mend ‘market failure’ so that the invisible hand of the market can create paradise for all, what use is a vote at nation state level? Further, if the ‘market’ can manipulate politicians in the shape of threats and bribes from powerful companies, where is the citizen to exercise any influence?

Many contend that for a variety of reasons democracy needs to mean more than churning almost identical politicians every few years²¹². The ability of such politicians to represent a wide range of possibilities has been severely eroded by a number of factors, some stemming from the ‘willing capture’ of the state²¹³, others from globalization²¹⁴ and the ability of

²¹⁰ . Beck, *Power in the Global Age*, Polity, 2005, page 52.

²¹¹ Beck, *Power in the Global Age*, page 79.

²¹² Teubner, G, argues that merely elevating actors such as MNEs into traditional governance is flawed as the designers “cannot free themselves of the fascination of nation-state architecture’ Societal Constitutionalism: Alternatives to State-centred Constitutional Theory,” Stoors Lectures, 2003/4 Yale Law School, p54

²¹³ . Dine *Companies, International Trade and Human Rights* CUP, 2005

multinational companies to evade and supersede state regulation²¹⁵. These twin forces mean that the state is ‘on the side’ of the multinationals and, if state authorities deviate from subservience to corporate interests they are able to evade regulation²¹⁶ or leave. One of the consequences of the overwhelming consensus about the ‘proper’ economic path to success which has loosely been labelled the ‘Washington Consensus’ has been the ‘dumbing down’ of politics to a narrow centrist band which is obsequious to ‘the market’ and consequently to large market players, most notably transnational corporations. This has led not only to the ‘market state’²¹⁷ but also to the fragmentation of power away from the traditional monolithic state structures. It has also led to the blurring of the boundaries between public and private realms, including public and private law.²¹⁸ Regional and international agreements have also achieved fragmentation.²¹⁹ This has made governance structures more complex and less responsive to democratic pressure. Power has become multicentric rather than monolithic²²⁰. Beck believes that “Globalisation . . . has introduced a new space and framework for acting: politics is no longer subject to the same boundaries as before”²²¹ For Beck the pieces of the jigsaw of global politics has been rearranged partly by multinational companies²²²

“The world to-day behaves like a madhouse. The worst of it is that the values we had more or less defined, taught, learned, are thought of as archaic as well as ridiculous. Respect for the world: who is that important to? The human being should be the absolute priority. And it isn’t. It’s becoming less and less so. It seems that it’s more important to reach Mars than prevent 13 million Africans dying of hunger. Why would I want to know if there’s water on Mars if we’re polluting the water here on Earth, doing nothing to avoid it? Priorities need to be redefined, but there’s no chance of redefining those priorities if we didn’t confront the

²¹⁴ Ochoa, Christiana, “The Relationship of Participatory Democracy to Participatory Lawmaking” in this collection of papers., Stiglitz, J., *The Price of Inequality*, Allan Lane, page 118 et seq.

²¹⁵ . Beck *Power in the Global Age*, Polity, 2005, page 52.

²¹⁶ Just one example is the extensive use of offshore tax havens; .Alldridge,P, and Mumford,Anna, “Tax Evasion and the Proceeds of Crime Act 2002” (2005) 25 *Legal Studies* 253

²¹⁷ Williams, Rowan, *Guardian*, 27th February, 2003.

²¹⁸ Teubner ,G, argues that private law has become simply ‘juridification of economic action’ G. Teubner “The public/private dichotomy: After the critique?” paper given at the European University Institute seminar “Governance, Civil Society and Social Movements,” 30th June 2007

²¹⁹ Bernard,N, *Multilevel Governance in the European Union*, Kluwer 2000,. Joerges,C, “Integration through de-legalisation? An irritated heckler.” Paper given at the European University Institute seminar “Governance, Civil Society and Social Movements,” 30th June 2007

²²⁰ Aarte- Schole, Jan, “From Statism to Polycentrism: Transformations of Governance and Democracy” in this collection of papers.

²²¹ . Beck, *Power in the Global Age*, Polity, 2005, page 3.

²²² . Beck, *Power in the Global Age*, Polity, 2005, page 52-3

need to know what democracy is. We live in a very peculiar world. Democracy isn't discussed, as if democracy had taken God's place, who is also not discussed."²²³ Perhaps the discussion should begin with the understanding that markets are not all-powerful; "Adam Smith's invisible hand – the idea that free markets lead to efficiency as if guided by unseen forces – is invisible, at least in part, because it is not there."²²⁴

Charles Tilly rejects the argument that it is possible to identify a 'borderline' between democracy and non-democracy by an assessment of chosen factors such as those identified by Freedom House.²²⁵ Instead, Tilly focuses his definition on state-citizen relations and argues that democracy is always in a state of dynamic movement with constant pressures towards democratization and de-democratization.²²⁶ "Democratization means net movement towards broader, more equal, more protected and more binding consultation. De-democratization, obviously, then means net movement towards narrower, more unequal, less protected, and less binding consultation."²²⁷ In seeking to uncover the causes of movement in either direction he argues that there is a crucial difference between *capacity* of states and the health of their democracy. Here, capacity relates to states' ability to implement their policies. "*State capacity means the extent to which interventions of state agents in existing non-state resources, activities, and interpersonal connections alter existing distributions of those resources, activities and interpersonal connections as well as relations among those distributions*"²²⁸ Democratization depends on a complex interaction between the democracy in the sense of broader, more equal, more protected and more binding consultation and capacity to deliver. Tilly's central tenet is that democracy cannot be measured in the traditional ways which employ *idealist*, *structuralist* or *instrumentalist* approaches²²⁹ These, he explains, as "democracy as an idea that someone (the Greeks)²³⁰ invented, starting a centuries-long effort to implement the idea. We might take the opposite tack, arguing that only the conditions of industrial capitalism could support broad, equal, protective, and mutually binding political relations between states and citizens. We might also think that competing models of government, once familiar to national elites, attracted different sorts of ruling classes, and that some of those chose dictatorship and others democracy."²³¹ Rather,

²²³ Saramago, Jose, Guardian 28/12/02.

²²⁴ Stiglitz, Guardian

²²⁵ www.freedomhouse.org, accessed 8th August 2007

²²⁶ .Tilly,C, *Democracy*, Cambridge University Press, 2007

²²⁷ Tilly *Democracy*, p14.

²²⁸ Tilly *Democracy* p16. italics in original.

²²⁹ Tilly *Democracy* p48, italics in original.

²³⁰ Although he points out that the Greeks were slave owners and excluded women from politics so the breadth of participation is extremely suspect.

²³¹ Tilly *Democracy*, p49

Tilly argues that attention should be paid to *processes* to identify the movement towards or away from democracy. The processes he identifies are “increasing integration of trust networks into public politics, increasing insulation of public politics from categorical inequality and decreasing autonomy of major power centres from public politics.”²³² The first of these and its relationship with his definition of democracy is encapsulated by the following; “of breadth, equality, mutually binding consultation and protection, integration of trust networks into public politics most directly affects mutually binding consultation. To the extent that people integrate their trust networks into public politics, they come to rely on governmental performance for maintenance of those networks. They also gain power, individual and collective, through the connections to government that those networks mediate. They acquire an unbreakable interest in governmental performance. The political stakes matter. Paying taxes, buying governmental securities, yielding private information to officials, depending on government for benefits, and releasing network members for military service cement that interest and promote active bargaining over the terms of its fulfilment.”²³³ Trust networks “contain *ramified interpersonal connections, consisting mainly of strong ties, within which people set valued, consequential, long-term resources and enterprises at risk to the malfeasance, mistakes, or failures of others.*”²³⁴

It is clear that the trust between citizens in Greece, Spain and the UK and their governments has recently been strained.²³⁵ However even before the financial crisis inequality, particularly in the US and the UK has damaged democracy. Tilly argues that it is possible to have significant inequality and rely on political magic tricks to isolate political decision making from that inequality by mechanisms which do not reflect those inequalities in formal arena. I have argued elsewhere that this is only true to a very limited extent. Those who are starving don't vote and even marginalisation can breed despair as having any influence. Where there is a dominant actor, such as the financial sector, governments are subordinated and unable to help its citizens. This is particularly cogent for the inequality debate. Inequality fuels de-democratizing forces, the poor often do not vote but society can be split by divisions between classes, a new Apartheid. Both Ehrenreich and Toynbee vividly portray the ‘invisibility’ factor as part of the experience of poverty due to low pay in the US and UK respectively²³⁶. Fallows notes the lack of shared spaces and services. In the US “As public schools and other public services deteriorate, those who can afford to do so send their

²³² Tilly *Democracy*, p50

²³³ Tilly, *Democracy* p95

²³⁴ Tilly *Democracy*, p81, italics in original

²³⁵ Bawdon, Fiona, “Verdict on UK Riot; people need a ‘state in society’, says report”, <http://www.guardian.co.uk/uk/2012/mar/28/verdict-uk-riots-stake-society>, <http://www.guardian.co.uk/world/greece>, Tremlett, Giles, “Spain reels at violent tactics by riot police”, <http://www.guardian.co.uk/world/2012/sep/29/spain-riot-police>, all accessed on 11/10/2012.

²³⁶ . Errenreich,B, *Nickel and Dimed* (Granta, London 2002, . Toynbee,P, *Hard Work*, Bloomsbury, London, 2003 and see Gear, *Redirection HR*, page 174

children to private schools and spend their off-hours in private spaces- health clubs, for example, instead of the local park. They don't ride on public buses and subways. They withdraw from mixed neighbourhoods into distant suburbs, gated communities or guarded apartment towers; they shop in stores that, in line with prevailing 'market segmentation' are designed to appeal to the affluent alone."²³⁷ Toynbee writes London was a sadder, duller, more impoverished place. . . . Wherever I walked, everything I passed was out of bounds, things belonging to other people but not to me. . . . This is what 'exclusion' means, if you have ever wondered at this modern wider definition of poverty. It is a large No Entry sign on every ordinary pleasure."²³⁸ This polarisation of society is neatly summed up in Klein's metaphor of *Fences and Windows* to describe the separation of the haves and have-nots (Fences) and the opportunities for hope (Windows²³⁹).

Such exclusion does not readily lead to political participation. Tilly apparently discounts the effects of the way in which inequality and discrimination is built into political systems in an institutional way, an issue discussed below in relation to institutional racism and corruption. Further, the third process identified by Tilly is the antithesis to the inequality issue. That third process is decreasing the autonomy of major power centres from public politics. A revealing part of the discussion of this issue comes when Tilly deals with the de-democratization of Russia by Putin "Yet in one regard Putin may surprisingly have been promoting longer-term changes that will eventually facilitate Russian democratization. Although he was permitting Russian military dangerously broad autonomy in the Caucasus, he was also subordinating capitalists who had acquired extraordinary independence from state control." Here Tilly has missed the point and appears to be operating in a pre-transnational corporate world. Corporations not only *Rule the World*²⁴⁰ but they have bought the politicians, if not with money then with economic argument and sheer economic power. The result of this is to corrupt the whole system. So democratization by decreasing the autonomous power of corporations can only come by accepting that what is required is an alternative approach to the economic system which decreases the reach of corporate power and its elites. This can only be achieved by popular pressure. It is therefore arguable that the US, UK and Europe have significantly de-democratized in recent years because of increasing inequality and because of the 'willing capture' by companies of the 'market state' giving significant autonomous power to corporations.

²³⁷ Ehrenreich *Nickel and Dimed*, p216, citing . Fallows,J, "The Invisible Poor", New York Times, March 19th 2000.

²³⁸ *Hard Work*, p239.

²³⁹ . Klein,N, *Fences and Windows*, Picador, New York, 2002. Klein argues that global society has created many fences; "barriers separating people from previously public resources" (pXVIII) both physical barriers and virtual ones such as education being restricted by the charging of fees. Windows are signs of hope of breaking down barriers such as the World Social forum and reclaiming public spaces.

²⁴⁰ . Korten,D, *When Corporations Rule the World*, Kumarian Press 1995, J. Pilger *The New Rulers of the World* Verso, London, 2002

The second process identified by Tilly as an indicator of democratization is equality “Democracy works better, and democratization is more likely to occur, when political processes, reduce translation of everyday categorical inequalities into public politics.”²⁴¹ Thus the argument is not that democracy cannot exist where there is significant inequalities but that these must not appear in the political arena. By categorical inequalities Tilly means “organized differences in advantages by gender, race, nationality, ethnicity, religion, community and similar categories.”²⁴² Democracy thrives on a lack of correspondence between the inequalities of everyday life and those of state-citizen relations”.²⁴³ “Any substantial increase in categorical inequality also affects democracy’s prospects. Any substantial increase in categorical inequality that occurs without some compensating adjustment in public politics poses a serious threat to existing democratic regimes.” . . .²⁴⁴

“ Increasing categorical inequality threatens democracy because it gives members of advantaged categories means and incentives to:

- * Opt out of democratic bargains
- * Create beneficial relations with state agents
- * Shield themselves from onerous political obligations
- * Use their state access to extract more advantages from unequal relations with non-state actors
- * Use their influence over the state for further exploitation or exclusion of subordinate categories, and thus
- * Move their regimes even further away from broad, equal, protected, mutually binding consultation”²⁴⁵

Here the Corporate Governance is key, company law, social movements, human rights activism and corporate social responsibility must go hand in hand with democracy and why the arbitrary distinction between Corporate Governance and Corporate social Responsibility should be demolished. This is particularly crucial because of the coming danger for the environment. The EU Aquis Communautaire should be truly a binding commitment to democracy not an administration of the Elites. Consensus politics as found in German could allow more participation in government and corporate governance.

²⁴¹ Tilly *Democracy*, p111

²⁴² Tilly *Democracy* p111

²⁴³ Tilly *Democracy* p118.

²⁴⁴ Tilly *Democracy*, p118.

²⁴⁵ Tilly *Democracy* p137.

The Environment and Corporate Governance.

For some time there has been a problem of pollution from companies because they are not internalizing their waste and costs. There is also no doubt that there has been a significant export of 'dirty' industries and significant pollution from the activities of mining and manufacturing operations masterminded by TNCs across the world. "One of the keys to understanding the global problem of waste and pollution, is that much of its incidence in the developing world is due to developed nations' illegal shipment of their own waste to these regions. . . trucks entering Eastern Europe [from Germany] export hundreds of thousands of tons of waste that Westerners find too expensive or too inconvenient to dispose of themselves. The pressure is mostly financial. Under US and European environmental laws today, the cost of disposing of hazardous industrial and mining waste can be as high as several thousand dollars per ton . . . Shipping such materials abroad is often much cheaper."²⁴⁶

The exporting nations can pose as environmentally aware:

"Japan has reduced its aluminium smelting capacity from 1.2 million tons to 149,000 tons and now imports 90% of its aluminium. What this involves in human terms is suggested by a case study of the Philippine Associated Smelting and Refining Corporation (PASAR). PASAR operates a Japanese-financed and constructed copper smelting plant in the Philippine province of Leyte to produce high grade copper cathodes for shipment to Japan. The plant occupies 400 acres of land expropriated by the Philippine Government from local residents at give-away prices. Gas and waste water emissions from the plant contain high concentrations of boron, arsenic, heavy metals, and sulfur compounds that have contaminated local water supplies, reduced fishing and rice yields, damaged the forests, and increased the occurrence of upper respiratory diseases among local residents. Local people whose homes, livelihoods and health have been sacrificed to PASAR are now largely dependent on the occasional part-time or contractual employment they are offered to do the plant's most dangerous and dirtiest jobs."²⁴⁷

David Leigh has written on the Trafigura disaster where a ship unloaded cargo in the Ivory Coast killing many and damaged at least 31,000. The ship was loaded with toxic chemicals from Europe: "The UN human rights special rapporteur, Professor Okechukwu Ibeanu, wrote: "According to official estimates, there were 15 deaths, 69 persons hospitalised and more than 108,000 medical consultations ... there seems to be strong prima facie evidence that the reported deaths and adverse health consequences are related to the

²⁴⁶ Czinkota, M, Ronksinen, I, and Moffett, M, *International Business* (4th ed, Dryden, 1996).

²⁴⁷ Korten *When Corporations Rule the World*.

dumping.”²⁴⁸ According to Leigh “The documents reveal that the London-based traders hoped to make profits of \$7m a time by buying up what they called "bloody cheap" cargoes of sulphur-contaminated Mexican gasoline. They decided to try to process the fuel on board a tanker anchored offshore, creating toxic waste they called "slops".²⁴⁹ A number of company internal e-mails were found: ‘One trader wrote on 10 March 2006: "I don't know how we dispose of the slops and I don't imply we would dump them, but for sure, there must be some way to pay someone to take them.’ The resulting black, stinking, slurry was eventually dumped around landfills in Abidjan, after Trafigura paid an unqualified local man to take it away in tanker trucks at a cheap rate”.²⁵⁰ Recently there is disquiet with ‘fracking’²⁵¹. There are many reports of environmental violations perpetrated by large companies.²⁵² Simultaneously the amount of extraction of minerals and other materials from the ground rises exponentially. “On the eve of India’s independence, Mahatma Gandhi was asked whether he thought the country could follow the British model of industrial development. His response retains a powerful resonance in a world that has to redefine its relation to the earth’s ecology: ‘It took Britain half the resources of this planet to achieve its prosperity. How many planets will India require for development?’ We ask the same question for a world edging towards the brink of dangerous climate change.

Climate Change

“There is “a looming environmental crisis, which poses a threat to the basic of our very existence”²⁵³ The IPCC believe “There is *high confidence* that neither adaptation nor mitigation alone can avoid all climate change impacts . . . Unmitigated climate change would, in the long term, be *likely* to exceed the capacity of natural, managed and human systems to adapt. Reliance on adaptation alone could eventually lead to a magnitude of climate change to which effective adaptation is not possible, or will only be available at very high social,

²⁴⁸ Leigh, David, “How UK oil company Trafigura tried to cover up African pollution disaster, Guardian 16/09/2009.<http://www.guardian.co.uk/world/2009/sep/16/trafigura-african-pollution-disaster>, accessed on 17/10/2012.

²⁴⁹ *ibid*

²⁵⁰ *ibid*

²⁵¹ <http://quitcoal.org/natural-gas-hydraulic-fracking>, accessed on 16/10/2012 “Hydraulic fracture methods (“fracking”) are associated with a range of environmental impacts, some of which are not fully understood. It’s possible that the carbon footprint of shale gas may be significantly greater than for conventional gas”.

²⁵² See Oxfam *Global Finance Hurts the Poor*, Oxfam America, Boston 2002 esp p 46 and Oxfam *Oil, Gaz and Mining: Poor Communities Pay the Price*: Oxfam America, Boston 2001.

²⁵³ Sjaffell, Beate, *Towards a Sustainable European Company Law*, Wolters Kluwer, 2009, page 3, Dieter Helm and Cameron Hepburn (Eds) *The Economics and Politics of Climate Change*, Oxford University Press, 2009.

environmental and economic costs.²⁵⁴ There has been for some time a pollution epidemic but the climate change crisis has eclipsed this. The corporate governance debate has not included the issues of climate change, rather shied away from internalizing environmental costs including carbon emissions. The sustainability industry is large but is beset by spin doctors.²⁵⁵ The Stern Review said that the negative effects of externalising greenhouse gasses is “the greatest and widest-ranging market failing ever seen”²⁵⁶ Using the annual ceiling of 14.5 Gt CO₂, if emissions were frozen at the current level of 29 Gt CO₂ we would need two planets. However, some countries are running a less sustainable account than others. With 15 percent of the world population, rich countries are using 90 percent of the sustainable budget. How many planets would we need if developing countries were to follow the example of these countries?²⁵⁷

At last we believe that anthropogenic is real: “we have slowly, and at times reluctantly, realised that humanity has become an active agent in the reshaping of physical climates around the world, so our cultural, social, political and ethical practices are reinterpreting what climate change means.”²⁵⁸ Principle 12 of the Rio Declaration requires states to cooperate to promote a supportive and open international economic system and demanded that “trade policy measures for environmental purposes should not constitute a means of arbitrary or unjustifiable discrimination or a disguised restriction on international trade”²⁵⁹ Agenda 21 of the Rio Declaration also says that international trade has been inequitable and this has been one reason for environmental degradation of the planet. It is a paradox that the Declaration also believed in the logic of trade liberalisation particularly because it would be good for the world. Elliott argues that one reason for the argument is a semantic one; the rhetoric of international trade does not allow ‘protection’ against nations. She says “Can environmental protection issues be accommodated within the logic of trade liberalisation? Can trade

²⁵⁴ IPCC Core Writing Team, R.K. Pachauri, R. K. and . Reisinger, A, (eds) *Climate Change 2007: Contribution of Working Groups I, II and III to the Fourth Assessment Report of The Intergovernmental Panel on Climate Change* (Geneva: IPCC 2008, http://www.ipcc.ch/pdf/assessment-report/ar4/syr/ar4_syr.pdf, accessed on 16th October 2012.

²⁵⁵ <http://www.eiris.org/files/research%20publications/EIRISGlobalSustainabilityReport2012.pdf>,

²⁵⁶ . Stern, N, on the Economics of Climate Change: Executive Summary 2006, www.sternreview.org.uk, accessed on 16/10/2012, see also N. Stern, *The Economics of Climate Change: The Stern Review*, Cambridge University Press, 2007,

²⁵⁷ United Nations Development Programme *How Many Planets*, <http://hdr.undp.org/en/statistics/data/climatechange/planets/>, accessed on 16/10/2012, Dieter Helm and Cameron Hepburn (Eds) *The Economics and Politics of Climate Change*, Oxford University Press, 2009.

²⁵⁸ Hulme, Mike, *Why we Disagree about Climate Change*, Cambridge University Press, 2009, page xxv,

²⁵⁹ UNCED 1992 *Report of the UN Conference on Environment and Development Annex I, Rio Declaration and Development*, A/CONE. 151/26 (Vol 1), 12th August.

liberalisation contribute to overcoming environmental degradation or is it likely to contribute to further environmental degradation? Is it possible in trade liberalisation discourse, to distinguish between environmental protection and environmental protectionism? . . . These are important because ‘trade rules and agreements are a major determinant of how natural resources are used, what pressures are placed on the environment and who benefits from the huge money flows. . . that cross borders with the exchange of goods . . . At a normative level, answers to these questions rest in part on different views about ‘protection’ – a ‘pejorative term’ for the trade community.’²⁶⁰ For corporate governance this matters because of the importance of the macroeconomic context where the WTO is crucial is heavily influenced by neo-liberal economics. Deregulation and free markets policies and environmental protection are usually conflicting aims, although some scholars believe that a market solution can be found. . Paterson promotes a privatized market mechanism arguing for a new paradigm known as ‘global environmental governance’ : “while such governance is commonly seen in terms of a tragedy of the commons arising out of the anarchy of the interstate system, it is more fruitful to analyse these dynamics in relating to a conception of global capitalism. While efforts to govern global environmental problems started out as attempts to regulate the side-effects of existing form of capitalism development, they have increasingly been organised to channel capitalism in novel directions.”²⁶¹ Indeed climate change is a new sort of ‘pure public commons’²⁶² Since no state or individual can fashion a solution. Although it is clear that that inter-state rivals can co-operate in treaties, accords and protocols.²⁶³ The power of ‘Capital’²⁶⁴ is so pervasive that even international law has been captured.²⁶⁵ Paterson shows that global governance has been guided by the Washington Consensus and the fetishism of markets today.²⁶⁶ Now privatisation has gone further, in a “dynamic change where standards and regulations are obeyed not by governments but in market rules by the market for the market”.²⁶⁷ Paterson believes that market mechanisms are “shaping business

²⁶⁰.Elliott, L, *The Global Politics of the Environment*, (second ed) Palgrave Macmillan, 2004, citing . Postel ,S, and Flavin ,C, , “Reshaping the global Economy” in Brown, Lester R, *et al*, (eds) *State of the World*, Norton & co, 1991 and . Berlin,K, and . Lang, T, *Trade and the Environment*, *The Washington Quarterly*, vol. 16, no 4 Autumn , pp35-51.

²⁶¹ Paterson, Mathew, “Global governance for sustainable capitalism? The political economy of global environment governance”, in , (Eds) I Adger,W. Neil, and Jordan,Andrew, *Governing Sustainability*, CUP 2009, page 99.

²⁶³ Brown, Katerina, “Human development and environmental governance: a reality check”, in. I Adger and Jordan,*Governing Sustainability*, CUP, 2009 and Mike Hulme *Why we Disagree About Climate Change*, CUP 2009.

²⁶⁴ Beck, U., *Power in the Global Age*, Polity Press, 2005.

²⁶⁵ Beck ibid and see Anna Gear, *Redirecting Human Rights*, Palgrave Macmillan, 2010. ,

²⁶⁶ Paterson, “Global governance for sustainability capitalism”. *Governance Sustainability*, 2009, page 107.

²⁶⁷ Paterson cites instances like the International Organisation for Standardization’s 1400014000, the Forest Stewardship Councils, id Page 109.

practice, potentially significantly. Should the variety of schemes to shape investment practice with regard to CO₂ emissions – the Carbon Disclosure, Project, the Global Reporting Initiative, UNEP’s Financial Industries Initiative, and so on – succeed in generating a norm which treats CO₂-intensive firms as financial liabilities, then substantial change in investment in renewable energy can be expected . . . But, on the other hand, privatisation not only entails firms attempting to self-regulate to organise and legitimate their growth, but environmental NGOs to fill the void left by declining regulation by states, through developing schemes to put pressures on firms to change practices²⁶⁸.” We will see whether these market solutions will work and change the complacency around the climate change debate and ameliorate carbon emissions and whether corporate governance can be part of this movement However, here are already a proliferation of Carbon Trading markets²⁶⁹ but many commentators believe that financial emission markets are only a way of making money rather than ameliorating the problem of climate change. “Alongside the development of proposals for emissions trading schemes at global and national level was a positive explosion of activity by financial markets actors . . . What explains this explosion of activity is that, while emissions trading can be understood in terms of economic efficiency, it very definitely operates through the creation of new markets in which firms can develop economic strategies and secondary markets. In fact, the future markets in this instance existed significantly before the real markets. . . Emissions trading as a project has been, and continues to be, propelled by realisation by powerful financial actors that here was a new commodity to be sold, new profits to be made”²⁷⁰ Similar projects are criticised in the some way, including the Joint Implementation and the Clean Development Mechanism²⁷¹. Corporate governance mechanisms could affect the implementation of sustainable business; so far there are lamentably few effective strategies.²⁷² This introduction has sketched some of the issues involving corporate governance in a global context. Now the national background will be considered. Although the sovereignty of states has been severely compromised recently, national governments have some power to act in regulating companies. Although there are growing international regulations to restrict emissions national corporate governance should also be part of the picture if the planet is to be saved. This would entail embedding environmental policies into corporate governance and probably this would mean that the neo-liberal model of corporate governance would have to be significantly amended.

²⁶⁸ Paterson “Global governance for sustainability capitalism”, *Governance Sustainability*, 2009, page 109-110.

²⁶⁹ Including the European Trading market, Australian, BP, etc see Pulver, S, ” Making sense of Corporate environmentalism: an Environmental contestation approach to analyzing the causes and consequences of the climate change policy in the oil industry”, *Organisation and Environment* 20, 2007, pages 1-40.

²⁷⁰ Paterson, “Global governance for sustainability capitalism”. *Governance Sustainability*, 2009, page 111-112.

²⁷¹ id

²⁷² Sands, P., *Principles of International Environmental Law*, Cambridge University Press, 2009, for an European perspective see Beate Sjafell, *Towards a Sustainable European Company Law*, Wolters Kluwer, 2009, especially on pages 227-228

