

PRIVATE AND PUBLIC CORPORATE REGULATORY SYSTEMS: DOES CSR PROVIDE A SYSTEMIC ALTERNATIVE TO PUBLIC LAW?

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ABSTRACT

CSR (Corporate Social Responsibility) is an increasingly important area of corporate and legal concern. In addition to problems defining the meaning of the term and understanding its implications, there is a lack of understanding about how it can, does, and should interact with law. This paper answers this gap using a method used in the sociology of law: systems theory. The paper argues that CSR can be understood as a response to social costs and law's apparent failure to curb those costs. It focuses the examination on social costs generated by large industrial organizations and how they are regulated by public and private regulatory systems. It concludes with an innovative suggestion integrating ideas from ecological economic systems with both new and traditional regulatory solutions.

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I. INTRODUCTION: UNDERSTANDING THE PROBLEM

Corporate Social Responsibility, “CSR”, is a rapidly growing area of corporate concern and investment. Businesses such as Microsoft, Wal-Mart, and Apple are all involved in and claiming CSR credentials, and the Big Four audit and corporate advisory firm, KPMG, has described it as “de facto business law.”¹ The United Nations, the world’s main international law-making body, has formalised CSR principles in the international sphere through its Global Compact.² A fundamental and critical question, however, remains unanswered: How does CSR interact with the other institutions and systems of society?

Although there has been significant discussion and debate about CSR as a management practice, there is limited legal analysis of the phenomenon of CSR as a guide to or regulator of corporate conduct, and more particularly, how that regulatory role interacts with the public regulatory role of law. This paper analyses the interaction of CSR as regulation and public law. It relies on a systems perspective to provide a more robust approach to the investigation, and to illuminate and explain both the phenomenon and its interactions.

¹ See, e.g., European Commission, Proposal for a Directive of European Parliament and of the Council on procurement by entities operating in the water, energy, transport and postal services sectors, COM (2011) 895 final; Proposal for a Directive of the European Parliament and of the Council on public procurement, COM (2011) 896 final. Of course, some EU countries have already done so. See Karin Buhmann, *Corporate Social Responsibility: What Role for Law? Some Aspects of Law and CSR*, 6 CORP. GOVERNANCE L. REV. 188 (2006). Corporate responsibility reporting has become de facto law for business. (2013). Ruben Zandvliet, *Corporate Social Responsibility Reporting in the European Union: Towards a More Univocal Framework*, 18 COLUM. J. OF EURO. L. (2011); Pall A Davidsson, *Legal Enforcement Of Corporate Social Responsibility Within The EU*, 8 COLUM. J. OF EURO. L. 529 (2002).

² United Nations Global Compact, <http://www.unglobalcompact.org/> (last visited Feb. 16, 2017).

Control of the corporation has long been contested. While in prior centuries the contest over corporate control was between secular and religious authorities, in the current context, the contestants are business actors and civil society. Indeed it may be said that although the history of corporate law post-1900 can be read in many ways, one reading of it is as a history of the contest between a wealthy minority seeking to maintain power and privilege, and a broader majority seeking to spread benefits more widely and constrain the negative externalities (i.e. social costs) of industrial activity.³ In this telling, the majorities have relied on the power of numbers to force change, while the minority have relied on the power of political connections which they have combined with promises of good behaviour and well-publicised philanthropy to resist the constraints and re-distributions sought by the majorities. From a political perspective, the concentrations of wealth and power of business has been viewed as anti-democratic in nature and the subject of scholarly investigation and debate for more than three quarters of a century.⁴ In such analyses, corporations have been a focal point of the contest.⁵

Such broad-brush strokes, of course, fail to take account of the subtleties and shifts in historic socio-political discourse, changes in the natural and social environments at a global level, and the impact of these shifts and changes on corporate practices, corporate control, and industrial activity.⁶ The point of this discussion, however, is that regulatory efforts aimed at the corporation and its control has a long and chequered history. The core contention is binary: On the one side is a broader progressive common concern focused on constraining corporate harms and distributing more widely corporate benefits. On the other side is a conservative approach that favours the elite and seeks to resist broader claims and to continue externalising costs while concentrating benefits utilising the corporation.⁷

It is critical to note at the outset, though, that the issue is not necessarily as framed—an issue of the corporation per se. Indeed, industrial activity was usually organised by way of trusts as opposed to corporations in countries like the

³ ROB MCQUEEN, *A SOCIAL HISTORY OF COMPANY LAW: GREAT BRITAIN AND THE AUSTRALIAN COLONIES 1854-1920* (2009); Paddy Ireland, *Shareholder Primacy and the Distribution of Wealth*, 68 *MODERN L. REV.* 49 (2005).

⁴ ADOLF A. BERLE & GARDINER C. MEANS, *THE MODERN CORPORATION AND PRIVATE PROPERTY* (Harcourt, Brace & World, eds. 1968). And of course, before then by Thorstein Veblen. See THORSTEIN VEBLEN, *THE HIGHER LEARNING IN AMERICA: A MEMORANDUM ON THE CONDUCT OF UNIVERSITIES BY BUSINESSMEN* (Hill & Wang eds., 1957 [1918]).

⁵ SARAH A. SOULE, *CONTENTION AND CORPORATE SOCIAL RESPONSIBILITY* (Cambridge University Press. 2009).

⁶ Ronald Chen & Jon Hanson, *The Illusion Of Law: The Legitimizing Schemas Of Modern Policy And Corporate Law*, 103 *MICH. L. REV.* 1 (2004).

⁷ Benedict Sheehy, *Corporations And Social Costs: The Wal-Mart Case Study*, 24 *J. L. & COM.* 1 (2004) [hereinafter *Wal-Mart*].

USA.⁸ Rather the issues to a large degree are those surrounding large industrial organisations more generally.⁹

The colloquial conflation of large industrial organisations and legal corporations confuses the analysis.¹⁰ In this regard, it is common to hear reference to “corporate social responsibility”,¹¹ “corporate excess” and “corporate irresponsibility.”¹² This conflation, however, not only fails to add clarity, it obscures the real issues. Accordingly, instead of pursuing a misguided focus on the corporation-cum-industrial organisation, this paper distinguishes carefully between the two. When large industrial organisations¹³ are the focus, the acronym “LIO” will be used. When the legal body of the corporation is intended, the term “legal corporation” is used with the adjective “legal” to emphasise the usage. While it is understood that most LIOs are organised as legal corporations, or indeed collectives of corporations, to conflate the two undermines the strength of the analysis. The separate issue arising from the LIO’s use of legal corporation is that the corporation not only forms the foundation for most LIOs and provides an organisational framework, but it increases exponentially the potential benefit as well as the negative costs of the LIO.¹⁴ Accordingly, the separate analysis of the legal corporation will be necessary.¹⁵ Before that can happen, however, a clearer understanding of the contest is necessary.

The issues under contest are three-fold. They can be characterised normatively as: (1) what should the purpose of LIO be? (2) in terms of distributions, who should get what benefits and who should bear what costs? And (3) who should have the right to make these purposive and distributive decisions?¹⁶ In other words, the concern is that one particular group of people is

⁸ For example, the USA’s anti-trust and combines movement, led by US Supreme Court Justice Brandeis, was focused on breaking up the trusts, which were harming the US society and economy. Philip Cullis, *The Limits of Progressivism: Louis Brandeis, Democracy and the Corporation*, 30 J. AM. STUD. 381 (1996).

⁹ See, e.g., S. Prakash Sethi, *Self-Regulation Through Voluntary Codes*, in GLOBALIZATION AND SELF-REGULATION: THE CRUCIAL ROLE THAT CORPORATE CODES OF CONDUCT PLAY IN GLOBAL BUSINESS (S Prakash Sethi ed. 2011); Prakash Sethi, *Standards for Corporate Conduct in the International Arena: Challenges and Opportunities for Multinational Corporations*, 107 BUS. & SOC. REV. 20 (2002).

¹⁰ Benedict Sheehy, *Conceptual Interfaces between CSR, Corporate Law and the Problem of Social Costs* (SSRN, Working Paper 2012) [hereinafter *Interfaces*].

¹¹ ANDREW CRANE ET AL., OXFORD HANDBOOK OF CORPORATE SOCIAL RESPONSIBILITY (Oxford University Press 2008).

¹² LAWRENCE MITCHELL, CORPORATE IRRESPONSIBILITY: AMERICA’S NEWEST EXPORT (Yale University Press 2001); Brian Jones, *Corporate Irresponsibility and Corporate Social Responsibility: Competing Realities*, 5 SOC. RESP. J. 300 (2010).

¹³ The term “industry” is used to mean an area of productive activity.

¹⁴ *Wal-Mart*, *supra* note 7.

¹⁵ *Interfaces*, *supra* note 10.

¹⁶ See generally KENT GREENFIELD, THE FAILURE OF CORPORATE LAW: FUNDAMENTAL FLAWS AND PROGRESSIVE POSSIBILITIES (University of Chicago Press 2005).

making decisions that have significant consequences for whole groups of other people who in turn have little or no representation at the decision-making table. These are the basic political questions of who should have decision-making rights within the LIO regarding issues such as employment terms and conditions, profit distributions, and waste disposal. Matters such as these are dealt with quite differently in other large groupings of humans. Essentially, the questions are about how to characterise the LIO and where to draw its boundaries—i.e. to decide who are insiders and have their values implemented and who will be external to the LIO and can be ignored.¹⁷ These are evidently political issues and like all political agendas have regulatory programs.¹⁸

One major set of private regulatory initiatives is aimed at industrial organisations. This set includes various industry focused private regulatory initiatives such as the chemical industry's Responsible Care¹⁹ program, the forest industry's Forestry Stewardship Council²⁰ and the jewellery industry's Kimberley Process,²¹ as well the broader industry wide ISO 26000²², and even the publicly sponsored private regulatory initiative, the UN sponsored GRI.²³ This group of private regulatory programs can be readily grouped together under the umbrella term CSR. The regulatory space around industrial organisations, however, is already dense with public law.²⁴ This observation of CSR as private regulation combined with the role of public law provides a framing of the issue as one of co-existing regulatory systems, and with both attempting to regulate LIO, this co-existence is a phenomenon under-theorised and unexplained in the literature. As noted, therefore, this paper explores and seeks to explain this phenomenon using systems theory.

Traditionally governments, dwelling of course in the public realm, have been the sole source of regulation in the social system.²⁵ This tradition, however,

¹⁷ Benedict Sheehy, *CSR, Theories of the Firm and Models of the Corporation* (SSRN, Working Paper 2012).

¹⁸ Benedict Sheehy & Donald Feaver, *A Normative Theory of Effective Regulation*, 35 U.N.S.W. L. J. 392 (2015) [hereinafter *A Normative Theory*].

¹⁹ The Chemical Industry's Commitment to Sustainability, EUR. CHEM. INDUS. COUNCIL, <http://www.cefic.org/Responsible-Care/> (last visited Feb. 16, 2017).

²⁰ FOREST STEWARDSHIP COUNCIL, <http://www.fsc.org/> (last visited Feb. 16, 2017).

²¹ THE KIMBERLY PROCESS, <https://www.kimberlyprocess.com/> (last visited Feb. 16, 2017).

²² ISO 26000 – Social Responsibility, INT'L ORG. FOR STANDARDIZATION, <http://www.iso.org/iso/home/standards/iso26000.htm/> (last visited Feb. 16, 2017).

²³ GLOB. REPORTING INITIATIVE, <https://www.globalreporting.org/Pages/default.aspx/> (last visited Feb. 16, 2017).

²⁴ From basic Corporations Law, to laws regulating product liability, working hours and safety, to laws environmental dumping and advanced finance, the corporation exists in a broad and dense system of laws.

²⁵ SOULE, *supra* note 5, at 30.

has been in decline over the recent decades for a variety of reasons.²⁶ After the collapse of Keynesian economics in the 1970s, governments were increasingly the subjects of business criticism generated by normative neo-classical economists, and as governments shifted toward neo-liberalism, they became increasingly reluctant to constrain business.²⁷ This trajectory has led to the decline of the welfare state and rise of the regulatory state,²⁸ and an increase in what political scientists refer to as “private politics”.²⁹ Finally, changes in thinking about the nature and possibilities of regulation³⁰ have led to the development of new forms of regulation including among others private self-regulation.³¹ This change in regulatory studies and practices amounts to what can be described as a revolution in regulation. In sum, at a basic level, these changes represent fundamental changes in society’s institutions and hence, the social system.

Turning attention to systems, a feature of all systems is that they rely on some form of regulation in order to operate.³² From a systems perspective, which shall be discussed in greater detail below, a regulatory subsystem³³ is necessary to control activity within a system to prevent its explosion or implosion. The regulatory subsystems control inputs, throughputs, and outputs. Further, they control the border between a system and its environment ensuring adequate transfers for sustaining the system, while preventing it from being overrun. That is, regulatory subsystems and their mechanisms and processes have both internally and externally focused activities and dimensions.³⁴

Bringing together these three issues and ideas—the control of LIO, new regulatory approaches, and systems thinking—permits new thinking about and

²⁶ Sol Picciotto, *Regulatory Networks and Multi-Level Global Governance*, in RESPONSIBLE BUSINESS: SELF-GOVERNANCE AND LAW IN TRANSNATIONAL ECONOMIC TRANSACTIONS (Olaf Dilling et al. eds., 2008). See generally OLAF DILLING, ET AL., RESPONSIBLE BUSINESS: SELF-GOVERNANCE AND LAW IN TRANSNATIONAL ECONOMIC TRANSACTIONS (Hart Publishing 2008).

²⁷ DAVID HARVEY, *A BRIEF HISTORY OF NEOLIBERALISM* (Oxford University Press 2005).

²⁸ Donald Feaver & Benedict Sheehy, *The Shifting Balance of Power in the Regulatory State: Structure, Strategy and the Division of Labour* (Forthcoming), 41 J. L. & SOC. 203 (2014).

²⁹ SOULE, *supra* note 5, at 30.

³⁰ Donald Feaver & Benedict Sheehy, *A Positive Theory of Effective Regulation*, 35 U.N.S.W. L. J. 961 (2015) [hereinafter *A Positive Theory*]; *A Normative Theory*, *supra* note 18.

³¹ BRONWEN MORGAN & KAREN YEUNG, *AN INTRODUCTION TO LAW AND REGULATION: TEXT AND MATERIALS* (Cambridge University Press 2007).

³² Luhmann’s “self-reflectivity” See Die Gesellschaft der Gesellschaft 757 (1997), in Marc Amstutz, *The Double Movement in Global Law: The Case of European Corporate Social Responsibility*, in KARL POLANYI, *GLOBALISATION AND THE POTENTIAL OF LAW IN TRANSNATIONAL MARKETS* 370, N. 48 (Christian Joerges & Jose Falke eds., 2011).

³³ GUNTHER TEUBNER, *JURIDIFICATION OF SOCIAL SPHERES: A COMPARATIVE ANALYSIS IN THE AREAS OF LABOR, CORPORATE, ANTI-TRUST, AND SOCIAL WELFARE LAW* (W. de Gruyter 1987).

³⁴ Benedict Sheehy, *Regulation by Markets and the Bradley Review of Australian Higher Education*, 52 AUSTRALIAN U. REV. 60 (2010).

evaluation of the public and private regulatory systems for the LIO. This shift of the discussion about the control of the LIO from the contest of the political sphere to the regulatory sphere leads to a re-framing of the basic issue. Whereas in the political sphere, the question is a power contest, from a regulatory perspective, the question is: how best to control the power generated and concentrated by the LIO and the LIO's use of the legal corporation without destroying its benefits?

There are two main approaches contending for regulatory control of (i) the LIO and (ii) collaterally the legal corporation. These are: a public law solution, which works through a combination of the laws of corporations, contract, tort, environment, and labour, and a private law solution in the form of CSR.³⁵ The efforts of these two regulatory initiatives do not coalesce. Different points of reference, different objectives, and different methods bring them into conflict.³⁶ There are two ways to consider the issue: 1) that CSR and law are competing, or 2) that they are symbiotic regulatory systems. This article explores these two approaches—public and private law—by examining the nature, strengths, weaknesses, and limitations of the two regulatory systems and the conflicts between them. It analyses this regulatory contest using systems theories. Systems theory, applied by Luhmann to social systems,³⁷ provides a way of understanding the structures and processes in society and as such, a way to examine and analyse the dynamic interaction between actors and subsystems within society. Applying Luhmann's theory to the problem at hand provides new insight, first into the nature of the problem and second, into how the private regulatory system of CSR might interact and contend with the public legal subsystem to regulate industry. Before turning to this examination and analysis, however, a better understanding of the problem being addressed by both public and private regulatory systems is necessary.

II. FRAMING THE PROBLEM

The three normative questions raised about LIO do not arise in a socio-historical vacuum. Rather, they reflect a set of broader concerns or problems. Although there is a lack of consensus on the nature of the problems, there is discussion about three interrelated phenomena and their related issues. These are: (1) the social and environmental consequences of industrialisation, (2) the political and economic consequences of LIO in which power is concentrated in the hands of a few, namely, that they would corrupt and run government for their

³⁵ SOULE, *supra* note 5, at 31-35.

³⁶ *Interfaces*, *supra* note 10.

³⁷ NIKLAS LUHMANN, *SOCIAL SYSTEMS* (J Berdnarz & D Baecker trans., Stanford University Press 1996).

own narrow benefit³⁸—a concern raised by Lincoln,³⁹ and (3) the role of the law and its legal person, the corporation.⁴⁰ The paper turns next to address each in turn.

a. Social Costs: Labour and Environment

The first issue, discussed in economic terms as negative externalities or social costs,⁴¹ refers to the harmful aspects of industrial production and particularly, those of the LIO.⁴² This facet of the debate can be conceived of politically as about who should bear the particular costs of industrial activity, as noted above, with the parties being private corporate interests on the one side and the general public on the other. These issues have been identified in the discussion of private politics as matters of LIO policy, products, and negligence.⁴³ These political questions first became an issue in the late 18th century with Speenhamland,⁴⁴ as the expansion of the economy led to merchants investing in fixed plant⁴⁵ and, in the 19th century, led to a broader social reform movement associated with the 7th Earl of Shaftesbury and the effort to reform working conditions for the working class. This shift toward reforming working conditions in factories,⁴⁶ mines,⁴⁷ chimneys⁴⁸ and elsewhere continued intermittently throughout the 20th century. More recently, large scale changes in work and business practices as a result of de-industrialisation in developed countries, has caused new types of workplace and consumer injuries mass pollution and other social costs which together are enlivening concern about social costs again in the early 21st century. These new social costs reflect, among other things, an extension of concerns about the consequences of globalisation stemming from the technological innovations and changes and their impacts on the natural and social environment of the last part of the 20th century.⁴⁹

³⁸ See, e.g., the discussion in GAR ALPEROVITZ, *AMERICA BEYOND CAPITALISM: RECLAIMING OUR WEALTH, OUR LIBERTY, AND OUR DEMOCRACY* (John Wiley & Sons 2005).

³⁹ “I see in the near future a crisis approaching that unnerves me and causes me to tremble for the safety of my country . . . corporations have been enthroned and an era of corruption in high places will follow, and the money power of the country will endeavour to prolong its reign by working upon the prejudices of the people until all wealth is aggregated in a few hands and the Republic is destroyed.” Letter from President Abraham Lincoln, to Col. William F. Elkins (Nov. 21, 1864).

⁴⁰ SOULE, *supra* note 5.

⁴¹ KARL POLANYI, *THE GREAT TRANSFORMATION* (Beacon Press 1944).

⁴² *Wal-Mart*, *supra* note 7.

⁴³ SOULE, *supra* note 5, at 54-64.

⁴⁴ POLANYI, *supra* note 41, at 78.

⁴⁵ *Id.* at 171-84.

⁴⁶ The Factory Act 1833 3 & 4 Will. IV c103, (Eng.).

⁴⁷ Mines and Collieries Act 1842 c. 99, (Eng.).

⁴⁸ Chimney Sweepers and Chimneys Regulation Act 1840 c. 96, (Eng.).

⁴⁹ There is a vast literature on these subjects of globalisation and its effects. See, e.g., JURGEN OSTERHAMMEL & NIELS P. PETERSSON, *GLOBALIZATION: A SHORT HISTORY* (Princeton University

According to Kapp, social costs are:

“all direct and indirect losses sustained by third persons or the general public as a result of unrestrained economic activities. These social losses may take the form of damages to human health; they may find their expression in the destruction or deterioration of property values and the premature depletion of natural wealth; they may also be evidenced in an impairment of less tangible values”⁵⁰

The nature and extent of externalities has increased exponentially in the present day with innovations like factory ships that deplete fish stocks of the oceans by making fishing and fish processing a more efficient and attractive business; the business take-over of the natural environment through such things as the manipulation and patenting of genes, its increased control over public dialogue through such things as concentration of ownership of mass media and telecommunications, control over democratic governments providing policy to government through business lobbying, think-tanks creating various pro-business legislation in the national sphere and in international trade regulations.⁵¹ These and other issues emanating from industrial activity have spread to all parts of the globe in terms of social and political activity, and in ultimate terms challenging the ecological and political foundations of human life on the planet.

This first set of problems, as noted, has been recognised for centuries and in response different regulatory solutions have been proposed with varying degrees of success. Regulatory solutions have been focused on the mitigation of the degradation of the natural environment and the social consequences of the commodification of labour⁵²—including the above noted efforts to limit exposure to harmful work environments and practices, and to improve working conditions generally. Recent regulatory solutions are essentially calls for changes in the organisation of work and a simultaneous reduction of the impacts of industrial production on the natural environment.

b. Concentrations of Wealth and Power

The second issue is more contentious. Whether one thinks the concentration of wealth and power is problematic depends on basic political

Press 2005). For the often over-looked issue that this is not the first globalisation, see A.G. HOPKINS, *GLOBALISATION IN WORLD HISTORY* (Random House 2002).

⁵⁰ K. WILLIAM KAPP, *THE SOCIAL COSTS OF BUSINESS ENTERPRISE* 13 (Michael Barrett Brown ed., 2nd ed., 1977), in Sebastian Berger, *K. William Kapp's Theory of Social Costs and Environmental Policy: Towards Political Ecological Economics*, 67 *ECOLOGICAL ECON.* 244, 245 (2008).

⁵¹ See KEVIN PHILLIPS, *WEALTH AND DEMOCRACY: A POLITICAL HISTORY OF THE AMERICAN RICH* (Broadway Books 2002).

⁵² POLANYI, *supra* note 41.

philosophies as much as it does on one's position relative to that concentration—or at least one's view of such. Unsurprisingly, those at the heart of the concentration, and those aspiring to or hopeful of achieving those positions,⁵³ may often be unlikely to see it as problematic. Further, those of a conservative mindset or libertarian political philosophy are less likely to oppose the concentration of wealth, believing in the virtue of the status quo or, in the case of libertarians, the virtue of the processes that led to the status quo.⁵⁴ However, parties committed to democratic political philosophies who believe a society - and particularly a democratic one - functions better when inequality is not dramatic, and those committed to egalitarian principles⁵⁵ are less likely to see these concentrations as unproblematic and more likely to see them as problems (or even social costs) to be addressed.⁵⁶ As Justice Louis Brandeis, put it “We may have democracy in this country, or we may have wealth concentrated in the hands of a few, but we cannot have both.”⁵⁷

The problem of wealth concentration has two aspects. First, as noted by Brandeis, it harms democratic societies, which are based on limited power inequalities.⁵⁸ Second, there is a concern about power concentrations as represented by LIOs, which control vast swathes of the planet, economies larger than the GDP's of many countries, and are outside of democratic control.⁵⁹ Indeed, there was a significant discussion in American law, politics, and society generally in the last century about LIO as one of the three main institutions dominating politics along with “big government” and “big labour”.⁶⁰ LIOs in such positions not only manifest the control of geography, ecology, and economic

⁵³ The Economist, ‘*Don't Look Down: The Poor like Taxing the Rich Less than You Would Think*’ (2011), available at <http://www.economist.com/node/21525851?frsc=dg>. (Research suggests that lower classes support tax cuts for the top 1% of the wealthy on the hope that they too will one day be part of the 1%.)

⁵⁴ ROBERT NOZICK, ANARCHY, STATE, AND UTOPIA (Basic Books 1974).

⁵⁵ JOHN RAWLS, A THEORY OF JUSTICE (The Belknap Press of Harvard University Press Rev. ed. 1999).

⁵⁶ See THOMAS PIKETTY, CAPITAL IN THE TWENTY-FIRST CENTURY (Belknap Press 2014); Spencer Overton, *The Donor Class: Campaign Finance, Democracy, And Participation*, 152 U. OF PA. L. REV. 73 (2004). For an interesting overview of the problem and an innovative approach, see Jeff Seward, Professor, Pacific University Oregon, Address at the Western Political Science Association: Inequality and Actually Existing Democracy: A New Framework of Analysis (Apr. 2012).

⁵⁷ Cullis, *supra* note 8, at 394. See Ian Ayres & Aaron S. Edlin, *Don't Tax the Rich. Tax Inequality Itself*, N.Y. TIMES, Dec. 18 2011 at A29.

⁵⁸ Seward, *supra* note 56.

⁵⁹ Colin Crouch, *CSR and Changing Modes of Governance: Towards Corporate Noblesse Oblige?*, in CORPORATE SOCIAL RESPONSIBILITY AND REGULATORY GOVERNANCE : TOWARDS INCLUSIVE DEVELOPMENT? (Peter Utting & José Carlos Marques eds., 2009).

⁶⁰ C.A. Harwell Wells, ‘*Corporations Law is Dead*’: *Heroic Managerialism, the Cold War, and the Puzzle of Corporation Law at the Height of the American Century*, 15 U. PA. J. BUS. L. REV. 305 (2013).

systems, but they also dominate the social sphere. They unilaterally control people's activities through structured work, population movements by shifting locales of work,⁶¹ and through their domination of culture,⁶² people's personal and collective preferences and aspirations.⁶³ For example, one important aspect of the marked shift in the political environment toward the right was in part in a response to business' recognition of the importance of control of mass media for the shaping of public dialogue, beliefs, and government policy.⁶⁴

c. Role of the Corporation and Law

The third issue, also contentious, concerns the role of law generally and the corporation specifically. One group sees the first two problems, those of externalities and concentrations, in terms of failure of public law.⁶⁵ That is, they believe that law has failed to live up to expectations:⁶⁶ it has failed in its mandate to protect society and the environment from the negative consequences of industrialisation and LIOs in particular. The other group, which opposes public control of matters currently in the private sphere, seeks to avoid this eventuality of public political determination to redistribute costs and benefits of industrialisation by extending the scope of LIO's responsibility,⁶⁷ to be co-extensive and co-terminal with the impacts of its activity.⁶⁸

In sum, at a more fundamental level, these problems can be characterised as problems that have arisen as a consequence of developments within the social system (i.e. the activities of society not concerned with production and distribution on profit bases), namely the freeing of the economic subsystem from the rest. This issue has been discussed in the political economy literature by Polanyi as a transformation in society,⁶⁹ and as an issue of the disembedded

⁶¹ POLANYI, *supra* note 41, at 96-105.

⁶² See, e.g., Daniele Conversi, *The Limits of Cultural Globalisation?*, 1 J. CRITICAL GLOBALISATION STUD. (2010).

⁶³ See, e.g., SHARON BEDER, *Global Spin: The Corporate Assault on Environmentalism*, in THE EARTHSCAN READER IN BUSINESS AND SUSTAINABLE DEVELOPMENT (Richard Starkey & Richard Welford eds., Earthscan Publications 2000) (discussing social and cultural domination by LIOs are exemplified by companies such as News Ltd, Disney Studios with its ubiquitous Mickey Mouse, MGM, Pixar Studios animations).

⁶⁴ *Id.*

⁶⁵ GREENFIELD, *supra* note 16.

⁶⁶ See NIKLAS LUHMANN, LAW AS A SOCIAL SYSTEM 142 (Fatima Kastner et al., eds., Klaus A. Ziegert trans., Oxford University Press 2004) (1993) [hereinafter LAW AS A SOCIAL SYSTEM].

⁶⁷ This group, usually business advocates, hold a benign view of industrial activity and concentrations.

⁶⁸ Compare NOAM CHOMSKY, PROFIT OVER PEOPLE: NEOLIBERALISM AND GLOBAL ORDER (Seven Stories Press 1999) (representing Noam Chomsky's concern with LIO's impact on democracy) with JEROL MANHEIM, BIZ-WAR AND THE OUT-OF-POWER ELITE: THE PROGRESSIVE LEFT ATTACK ON THE CORPORATION (Lawrence Erlbaum Associates 2004) (attacking "anti-corporate" activists).

⁶⁹ POLANYI, *supra* note 41.

economy in the sociology of economics literature.⁷⁰ The social and economic system issues may be viewed and addressed in the first instance through systems theory.

Systems theory is outside the expertise of most law scholars and accordingly a brief introduction is presented next to assist the reader. After that brief introduction, the approach is applied to the problems just discussed.

III. SYSTEMS AND INSTITUTIONS: SOCIAL, POLITICAL, LEGAL, AND ECONOMIC

The issues under discussion can be analysed both through systems theory and institutionalist lenses. Indeed, given the nature of the phenomena, it is impossible to address the issue without both perspectives. Systems do not exist without actors, and in the larger context of social systems, the main actors are organisations. These organisations interact with each other and through these interactions develop institutions. Organisational interaction with other organisations and institutions can be characterised as a type of structuration at a systems level of analysis. In the context of developments of global social, economic, and political systems, the main organisational actor is the LIO. It has the least diversity in types of powerful constituents and the least politics, and hence is most able to develop and focus on advancing a more unified, coherent political agenda. This characteristic makes it a particularly powerful actor in the overall social sphere, which is populated by a variety of types of actors with conflicting agendas, multiple norms, and constituents.

LIOs hold immense sway over the distribution of power and other resources, and indeed, a select group of a few hundred tightly networked LIOs dominate the global economy.⁷¹ It is naive to suppose that these leviathans simply exert uncontaminated economic power without an eye to controlling the economic, political, and legal environments in which they operate.⁷² It could well be argued that the LIOs were under poor management if they were to fail to exert influence on their operating environments.⁷³

Nevertheless, the relationship between organisations, institutions, and systems is unclear. At a theoretical level, there is a conflict between incommensurate theories of systems, organisations, and institutions. Accordingly, some discussion of method is in order before we turn to deal with the issue at hand—the public and private regulatory systems dealing with LIO.

⁷⁰ Mark Granovetter, *Economic Embeddedness*, in CONTEMPORARY SOCIOLOGICAL THEORY (Craig Calhoun et al., eds., 2007 [1985]).

⁷¹ Stefania Vitali et al., *The Network of Global Corporate Control*, 6 PLOS ONE (Oct. 26, 2011), <http://journals.plos.org/plosone/article?id=10.1371/journal.pone.0025995/>.

⁷² STEPHEN WILKS, *THE POLITICAL POWER OF THE BUSINESS CORPORATION* (Edward Elgar 2013).

⁷³ Michael E. Porter, *The Competitive Advantage of Nations*, HARV. BUS. REV. (Mar/Apr, 1990).

Systems theory in broadest terms posits systems as a set of interacting, interdependent components. As a non-reductionist approach to complex problems, systems theory provides an approach to dynamic and complex phenomenon, including social systems.⁷⁴ Nikolas Luhmann, who first applied systems theory—a theory developed in natural sciences—to social phenomenon, took his analyses further and applied it to law, examining law’s characteristics as a subsystem of the larger social system.⁷⁵ Systems, according to Luhmann, have three features: they must be able to understand their own function in relation to the whole; they must be able to observe other systems and so be able to gauge their performance; and third, they must be able to observe themselves. Luhmann termed these features *function*, *performance*, and *self-reflexivity*.⁷⁶ Luhmann believed systems could be self-generating and would naturally tend to be self-regulating on the basis of these three features as systems are always embedded in environments.

Applying Luhmann’s three features to the social system generally, it is assumed that the function of the social system is to sustain human life on the planet. This norm underpins his first feature—system “*function*.” Everything, including subsystems such as the legal and economic subsystems must be understood and analysed in relation to its function in supporting the achievement of the objective of the larger function of the social system—“ensuring the satisfaction of future social needs”.⁷⁷ In such an analysis, it is clear that the function of each subsystem subsumes a particular set of norms—from biological sustenance in the case of the ecology, to social order in terms of law, to production and distribution on the basis of profit as norms of a capitalist economic subsystem.

The feature of system analysis examines each subsystem in relation to other subsystems, the feature Luhmann refers to as “*performance*.”⁷⁸ How a subsystem performs depends on how it interacts with adjacent subsystems. It may encroach upon, retreat from, interact symbiotically, interact parasitically, or become prey. Society functions with a higher degree of stability to the extent that

⁷⁴ ERVIN LÁSZLÓ, *THE SYSTEMS VIEW OF THE WORLD* (George Braziller 1972).

⁷⁵ Niklas Luhmann, *Symposium: Law and Social Theory: Law as a Social System*, 83 NW. U. L. REV. 139, 179 (1988-89) [hereinafter *Law and Social Theory*].

⁷⁶ See *Die Gesellschaft der Gesellschaft 757* (1997), in Marc Amstutz, *The Double Movement in Global Law: The Case of European Corporate Social Responsibility*, in KARL POLANYI, *GLOBALISATION AND THE POTENTIAL OF LAW IN TRANSNATIONAL MARKETS* 370-71 (Christian Jorges & Jose Falke eds., 2011).

⁷⁷ NIKLAS LUHMAN, *FUNKTION DER RELIGION*, cited in Gunther Teubner, *Corporate Fiduciary Duties and Their Beneficiaries: A Functional Approach to the Legal Institutionalization of Corporate Responsibility*, in *CORPORATE GOVERNANCE AND DIRECTORS’ LIABILITIES: LEGAL, ECONOMIC AND SOCIOLOGICAL ANALYSIS ON CORPORATE SOCIAL RESPONSIBILITY* (Klaus J. Hopt & Gunther Teubner eds., 1984).

⁷⁸ *Id.* at 163.

the subsystems are in stable, symbiotic relationships. Changes and upheaval in society can be explained as, or by reference to, subsystem performance, described more recently by systems thinkers as “*crisis*”.⁷⁹ The final feature for analysis is each subsystem’s “*self-reflective*” activity. This activity occurs as a subsystem evaluates its activity and restrains itself to avoid undermining the differentiated, neighbouring specialised subsystems on which it, they, and the overall system rely.⁸⁰

This self-reflective activity is the regulatory function within a system. Luhmann understood this issue as problematic in relation to the legal subsystem. He wrote:

“To clarify at the outset that the relationship of this [legal] system with the all-embracing social system is ambivalent. On the one hand society is the environment for its legal subsystem; on the other hand, all operations of the legal subsystem are always also operations in society, that is, operations of the society. The legal subsystem performs in society by differentiating itself within the society. In other words, the legal subsystem creates its own territory by its own operations. . . Only when doing so does it develop a social environment of law within society.”⁸¹

In other words, as legal language spreads law through a society, so too does economic language - and particularly its use in law - spread economic norms through the legal subsystem.

At this point, I wish to depart from Luhmann’s view of the legal subsystem and social theory in two important ways. First, Luhmann views the subsystem as having distinctive internal logics—that is, what is logical in one system may be illogical in another— which organise their own concerns internally and exclude other subsystems’ logics and complexities,⁸² – keeping in mind that subsystems are not visible to other particular systems and simply form part of the broader environment. The perspective taken in this paper sees the subsystems as having boundaries that are not apolitical and autopoietic subject to hard operative closure, but taking Luhmann seriously, as cognitive⁸³ and hence

⁷⁹ Marc Amstutz, *Eroding Boundaries: On Financial Crisis and an Evolutionary Concept of Regulatory Reform*, in *THE FINANCIAL CRISIS IN CONSTITUTIONAL PERSPECTIVE: THE DARK SIDE OF FUNCTIONAL DIFFERENTIATION* (Poul F. Kjaer et al., eds., 2010).

⁸⁰ *Law and Social Theory*, *supra* note 75, at 180-81.

⁸¹ *Id.* at 73.

⁸² Luhmann sees subsystems as developing operative closure through reducing complexity internally through organising phenomena while excluding other complex phenomena not susceptible to its own classifications. *LAW AS A SOCIAL SYSTEM*, *supra* note 66, at 475.

⁸³ NIKLAS LUHMANN, *SOCIAL SYSTEMS* ED.xxiii-xxiv 457 (John Berdnarz, Jr. & Dirk Baecker trans., Stanford University Press 1996).

contested, and encroachable, particularly where language is shared. That is, systems are taken as being susceptible to invasion, co-option, subversion, and collapse where they share particular phenomena and descriptors of such. It is not that Luhmann does not see this possibility—he does⁸⁴—however, Luhmann describes it in as an evolutionary or adaptational matter of one subsystem adopting norms of another subsystem rather than the result of political contest.⁸⁵

Teubner has addressed the issue of subsystems overreaching and harming neighbouring subsystems, which with respect to the legal subsystem he describes as creating a “regulatory trilemma.”⁸⁶ The trilemma is that law may be irrelevant to the neighbouring systems, may damage neighbouring subsystems by over-legalising them, or may be over-socialised itself, thereby destroying its self-reproductive ability.⁸⁷ In Teubner’s terms, the latter leads to a “juridification of the social spheres.”⁸⁸ While Teubner’s concern has been how the legal subsystem interacts with neighbouring subsystems, Luhmann’s vision of the legal subsystem as an autopoietic normative system, making blind determinations of what falls within and what is excluded⁸⁹ ignores the political determination and regulation of the boundaries of the subsystems, and leaves a marked gap in his analysis.⁹⁰ And this gap is the second differentiation of this work from Luhmann—i.e. that Luhmann does not see an overall regulatory system at work mediating between subsystems or policing borders.⁹¹ As just noted, Teubner sees this potential

⁸⁴ For example, in discussion systems self-reproduction, Luhmann observes that it does not always go well. These reproductions he describes as “deviant self-reproductions”. *Id.* The method of encroachment can be explained in Luhmann’s system this way.

⁸⁵ LAW AS A SOCIAL SYSTEM, *supra* note 66, at 142-72. Explained in a succinct if summary form, in Introduction, Richard Nobles and David Schiff, *in id.* at 10-11. I am not arguing that Luhmann is wrong in his argument. Indeed, the analysis which follows supports this view. For example, law has adopted economic language particularly in corporate law in the Australian CLERP discussed below, or the adoption of contract language favoured by economics for the corporation, while manifestly inadequate, as demonstrated by Hayden in the High Court, and failing to distinguish between economists’ use of the term and legal uses. Thomas W. Joo, *Contract, Property, and the Role of Metaphor in Corporations Law* 35 UC DAVIS L. REV 779 (2002). And in that same instance, the economists use of the language of “contract” but meaning something other than a legally enforceable agreement and “firm” not meaning a partnership all have reshaped law’s understanding and use of the terms. The use of terms like “citizen”, “consumer” likewise have been used to create confusion.

⁸⁶ Gunther Teubner, *After Legal Instrumentalism: Strategic Models of Post-Regulatory Law*, in *DILEMMAS OF LAW IN THE WELFARE STATE* 6 (Gunther Teubner ed. 1986).

⁸⁷ TEUBNER, *supra* note 33, at 22-27.

⁸⁸ *Id.*

⁸⁹ See LAW AS A SOCIAL SYSTEM, *supra* note 66, at ch. 2.

⁹⁰ See Saltman’s critique of Luhmann. MICHAEL SALTMAN, *THE DEMISE OF THE REASONABLE MAN: A CROSS-CULTURAL STUDY OF A LEGAL CONCEPT* 140-43 (Transaction Publishers 1991).

⁹¹ This view is not problematic in Luhmann’s theory which takes biology as its starting point and rejects (with good reason) the hierarchical model of government drawn from Europe’s history. LAW AS A SOCIAL SYSTEM, *supra* note 66. There is an irony that while economists interested in

problem.⁹² Again, it is not that Luhmann does not see the function of the legal system as regulatory, he does. He sees it in this regard as “a regulatory mechanism, serving the adaptation of society to its environment.”⁹³ However, in his view of law so functioning, Luhmann does not see it as regulating other subsystems. Rather, he sees it as forming part of the environment of other subsystems, influencing them, but no more.⁹⁴

The paper next turns to bring a systems approach to bear on the problems identified—social costs, concentrations of power and wealth, and the role of law.

IV. A SYSTEMS UNDERSTANDING OF THE PROBLEM OF SOCIAL COSTS, CONCENTRATIONS, AND LAW

In terms of the problem at hand—i.e. regulation of LIO—the issue can be characterised as the meeting of three subsystems, namely: economic⁹⁵, law, and politics—all housed in the social system which in turn finds its context in the ecology. (See Figure 1 below) The problems of the intersections of these three systems—i.e. the performance and function aspects—have been exacerbated first by the legal corporation, and second, in the current era of globalisation⁹⁶ by new developments in their interaction, new problems, and a re-defining of boundaries.⁹⁷

ecological systems call for a regulatory authority to control of human exploitation of ecological systems, ELINOR OSTROM, *GOVERNING THE COMMONS: THE EVOLUTION OF INSTITUTIONS FOR COLLECTIVE ACTION* (Cambridge University Press 1990). Luhmann who bases his theory of human society on ecology does not.

⁹² POUL F. KJAER ET AL., *THE FINANCIAL CRISIS IN CONSTITUTIONAL PERSPECTIVE: THE DARK SIDE OF FUNCTIONAL DIFFERENTIATION* (2010).

⁹³ LAW AS A SOCIAL SYSTEM, *supra* note 66, at 465.

⁹⁴ LAW AS A SOCIAL SYSTEM, *supra* note 66, at 466.

⁹⁵ In this article, I use the term “economic subsystem” to continue with the conventions of systems discussion. However, this understanding of the economic subsystem is quite distinct from the understanding of the economic subsystem as the interaction of rational actors seeking to maximise utility at the margins, as per neo-classicists. E. Roy Weintraub, *Neoclassical Economics*, THE CONCISE ENCYCLOPEDIA OF ECONOMICS, <http://www.econlib.org/library/Enc1/NeoclassicalEconomics.html>. This latter view of the economic subsystem denies or ignores the critical role of social institutions—such things as law and its equitable principles, and ethics. This institutional support is more readily captured by the term “business system” which of course includes economic norms and concerns such as production, resource allocation on rational grounds of utility and efficiency, and it also takes account of social norms and institutions including politics and other types of human behaviour which are inadequately treated in orthodox neo-classical economic analysis. From a functional perspective, business is a system within contemporary society which produces and distributes goods and services. It does so via markets organised on profit norms. The business system then bridges the broader social norms and the economic subsystem.

⁹⁶ Amstutz, *supra* note 79, at 365-85.

⁹⁷ Peer Zumbansen, *Law’s Knowledge and Law’s Impact: Reflections from Legal Sociology and Legal Theory*, 10 GERMAN L. J. 417, 419, n. 9 (2009).

Not only are the boundaries of the subsystems re-drawn, as is evident from neoliberalism's changed conceptions of public and private where the market has become the metaphor for all things private and the government re-defined as the regulatory state,⁹⁸ but the overall system function has been re-cast. The core of the problem is twofold. First, the economic subsystem has been re-cast as the whole of the social system, its norms as superior and all other subsystems as subordinate to it. In a theoretical analysis of the conflict between legal subsystem and the economic subsystem, this re-positioning of the economic has been described as follows: "[economics] not only seeks to reduce all legal decisions to calculations of utility, but also assumes that all of the activity surrounding law is economic in nature."⁹⁹ Second, economics' normative project and the resulting crowning of wealth as the ultimate value has reshaped society to devalue all else in relation to wealth. As a result, economic pursuit of wealth has become a significant normative driver of human behaviour in society.¹⁰⁰

An example of the economic subsystem's invasion of neighbouring subsystems is the shift of the overall function of the social system from saving and preserving for the next generation, as suggested by Luhmann, to economic growth based on consumption driven by the current generation.¹⁰¹ It may be argued that the roles of the subsystems are undergoing dramatic reform as a result of the dynamics introduced by an unregulated and disembedded economic subsystem.¹⁰² Obviously, the unregulated economic subsystem acts without regard for the ecology. Polanyi puts it sharply as: "from the denudation of forests, from erosions to dust bowls, all of which, ultimately, depend upon the [economic] factor land, yet none of which respond to the supply-and-demand mechanism of the market"¹⁰³ –albeit in a different argument. In other words, the ecology does not respond to economic supply and demand functions found in markets. Rather, the ecology operates on its own bio-geo-climatic systems. Clearly, a better framework for discussing such issues is a Social-Economic subsystems (SES) framework, discussed below.

The economic subsystem's encroachment upon the legal subsystem can be seen in the implementation of economic language in law—i.e. communication. In the law academy, the Law and Economics movement has taken up not only the method, but also the ideology of economics¹⁰⁴ and its core value of efficiency. It

⁹⁸ HARVEY, *supra* note 27, at 65.

⁹⁹ Nobles & Schiff, *supra* note 85, at 4.

¹⁰⁰ Fabrizio Ferraro et al., *Economics Language and Assumptions: How Theories Can Become Self-Fulfilling*, 30 ACAD. OF MGMT. REV. 8 (2005).

¹⁰¹ DAVID C. KORTEN, *WHEN CORPORATIONS RULE THE WORLD* (Kumarian Press 1995).

¹⁰² POLANYI, *supra* note 41; Granovetter, *supra* note 70.

¹⁰³ POLANYI, *supra* note 41, at 193.

¹⁰⁴ The response that economics is science and not properly called ideology ignores the facts of both science and economics. See DANIEL HAUSMANN, *THE INEXACT AND SEPARATE SCIENCE OF ECONOMICS* (Cambridge University Press 1992).

attempts to shift the goals and methods of law from equity and doctrine to efficiency, and makes an effort to make economic principles the main path of law.¹⁰⁵

The economic subsystem has also colonised the political system, or perhaps more accurately, developed using in its symbiotic relationship based on shared liberal political philosophy and neoclassical economic theory.¹⁰⁶ Both systems when based upon liberalism, view the unit of analysis as rational, independent, self-made individuals without society or community. As a result, investment in society or communal living is attacked whereas the commoditisation and privatisation of those commodities are seen as inherently desirable manifestations of individual's meritorious decisions. This reciprocal cycling of ideas has led to the encroachment and domination of the political landscape by the economic subsystem.¹⁰⁷

The criticisms of government, even by businessmen favouring CSR, are instructive. Hawkins, for example, writes: "In many cases governments fail to negotiate conclusions to disputes based on ideology whereas in business there is generally a compromise and deal to be made."¹⁰⁸ This criticism is misdirected because government and business have different goals—one is to make a profit, the other is to govern a society for its collective well-being. This prioritisation of economic norms is precisely the issue behind the failure of Habermas' discursive democracy.¹⁰⁹ Essentially, Habermas saw democracy developing out of a dialogue, informed by participants' views being shared, refined, restated, and ultimately adopted. If Habermas' ideal fails to materialise, what is left is likely to be something closer to the lowest common denominator of the competing values—i.e. the economic.¹¹⁰

One example of the encroachment by the economic system on the political can be seen in the institutionalisation and dominance of cost-benefit analysis in policy. At first, such analysis was but one of a variety of measures, which itself is an implicit acknowledgement that benefits tend to be more widely distributed and hence more difficult to measure, while costs are clear and quantifiable immediately. Now, cost-benefit analysis has become determinative of whether or not measures will be taken. In Australia, a federal government department, the Department of Finance and Deregulation, is dedicated to this task

¹⁰⁵ See, e.g., RICHARD POSNER, *THE ECONOMICS OF JUSTICE* (Harvard University Press 1983).

¹⁰⁶ For a discussion of the problem from an economic viewpoint, see Robert Ashford, *Milton Friedman's Capitalism and Freedom: A Binary Economic Critique*, 44 J. ECON. ISSUES 553 (2010).

¹⁰⁷ Ferraro et al., *supra* note 100.

¹⁰⁸ DAVID HAWKINS, *CORPORATE SOCIAL RESPONSIBILITY: BALANCING TOMORROW'S SUSTAINABILITY AND TODAY'S PROFITABILITY* 64 (Palgrave 2006).

¹⁰⁹ Jürgen Habermas, *Three Normative Models of Democracy*, 1 CONSTELLATIONS 1 (1994).

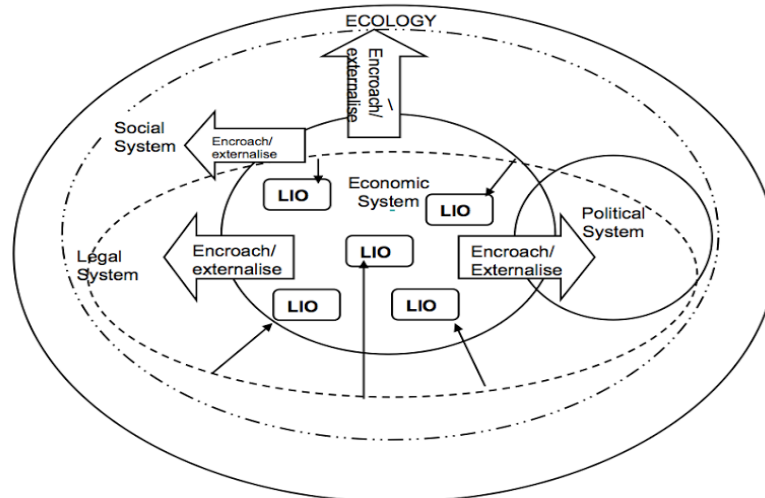
¹¹⁰ Marc Amstutz, *The Double Movement in Global Law: The Case of European Corporate Social Responsibility* (2011).

and favours the economic subsystem's goals over other important social projects. In the same country, a decade series of corporate law reform known as the Corporate Law Economic Reform Program was driven on the basis of economic norms. An example of the same phenomena in operation in the political sphere, where the political subsystem is seen as subordinated to and little more than essentially an underpinning of the economy, is evident in some of Bill Clinton's communications. His explanation to a journalist of his campaign was: "it's the jobs, stupid" and at another point in more colourful language: "'You mean to tell me that . . . my re-election hinges on the Federal Reserve and a bunch of fucking bond traders?'"¹¹¹

It is not that economic analysis is blind to the issue. Indeed, it is well known to economists¹¹² and is the subject of a large body of literature. Ultimately, the concerns about social costs are dealt with by other parties external to the transaction through extending property rights,¹¹³ or in law and economics views of the corporation, extending contracting,¹¹⁴ or taxation¹¹⁵—again assuming negotiations concerning tax too are conducted between equals seeking to address public social costs as opposed to maximising private wealth.

This broad set of problems can be illustrated graphically in the following diagram, Figure 1.

Figure 1: Systems in contest



Legend

Legal System - - - - -

Social System

¹¹¹ MICHAEL FOLEY & JOHN E. OWENS, CONGRESS AND THE PRESIDENCY: INSTITUTIONAL POLITICS IN A SEPARATED SYSTEM 204 (Manchester University Press 1996).

¹¹² *Wal-Mart*, *supra* note 7.

¹¹³ R.H. Coase, *The Problem of Social Cost*, 3 J. L. & ECON. 1 (1960).

¹¹⁴ F.H. EASTERBROOK & D.R. FISCHER, THE ECONOMIC STRUCTURE OF CORPORATE LAW (Harvard University Press 1991).

¹¹⁵ Chen & Hanson, *supra* note 6.

Figure 1 illustrates the systems under consideration. The whole of social activity, the social system, exists within the ecosphere. Accordingly, the ecological system functions in accord with laws of biology and is the ultimate system, which surrounds all others and in which all others exist and upon which all others rely. The social system, represented by a dash-dot line, rests within the ecological system and it contains all other subsystems. Its function of facilitating the survival of human society is coincident with its norm of social existence, which also operates as a *ground norm*¹¹⁶ for all other systems.

The interaction and interfacing of the other subsystems is somewhat more complex. The political system, with its norm and power, operates within the social system—and it functions as the creator and distributor of governance power among the population.¹¹⁷ It is socially embedded and is to some degree regulated by the legal subsystem—the rule of law ideal.¹¹⁸

The legal subsystem, represented by a dotted line, functions as a normative regulator of power. It is the political and works by prohibiting a society from ruling on the basis of violent power and instead inserting other values. These can be political ideologies, religion, or values such as equity. The legal subsystem extends beyond both business and politics into larger society, and even possibly into the ecosphere where one wishes to attribute rights to forms of life other than humans.

Lastly, the economic subsystem, which is not contained by the legal subsystem or the political, but extends beyond both, is represented as encroaching on neighbouring systems. When subsystems encroach on adjacent subsystems crisis may ensue.¹¹⁹ Indeed, it has been argued that the financial collapse and ensuing crisis of 2008 is the consequence of this encroachment.¹²⁰

The discussion of the diagram thus far leads to a consideration of the economic subsystem's prime actors, the LIOs, as represented by the boxes. The LIOs occupying legal corporations—i.e. the intersection of economic and legal subsystems—are connected to the legal subsystem by way of arrows, which

¹¹⁶ Kelsen's idea of the normative foundation of a legal subsystem, is the pre-legal grund norm. By using it in this context, I am arguing that the grund norm of the legal subsystem must be that which permits and sustains social existence. HANS KELSEN, *GENERAL THEORY OF LAW AND STATE* (Anders Wedberg trans., Russell & Russell 1961).

¹¹⁷ For argument illustrating interaction between political and legal power at the highest levels, see Benedict Sheehy & Donald Feaver, *Re-Thinking Executive Control of and Accountability for the Agency*, 54 *OSGOOD HALL L. J.* 175 (2016).

¹¹⁸ Luhmann comments on the difficulties associated with differentiating the political and legal subsystems. He writes that they are distinct in that while the political systems wields power, the legal subsystem wields norms and creates expectations. *LAW AS A SOCIAL SYSTEM*, *supra* note 66, at 162-65; Benedict Sheehy, et al., *Can CSR be Consistent with the Economic Model of the Firm?*, SSRN ELIBRARY (2011).

¹¹⁹ Amstutz, *supra* note 79.

¹²⁰ See KJAER ET AL., *supra* note 92, at xv-xx.

indicate that connection. As part of the economic subsystem these organisations extend their reach through the rest of society's systems and the ecology. The diagram illustrates how the economic subsystem encroaches on other neighbouring subsystems. While in Luhmann's view, the legal system has a significant temporal dimension, an "immunisation"¹²¹ of society against undesirable futures and against anticipated possible conflicts.¹²² A different orientation sees the function of the public legal subsystem as enacting, maintaining, and adjudicating¹²³ the political determination of the limitations, boundaries, or powers¹²⁴ of the differentiated subsystem within a society. In this sense, it is possible to talk about subsystems encroaching or over-powering neighbouring subsystems, and to speak of subsystem failures, as political acts and with their systemic consequences. Further, it allows such changes to be discussed as not simply the disembodied re-opening of subsystems which have achieved operative closure, but equally and perhaps more enlighteningly, be described as a political movement seeking to shift costs and benefits, re-embedding industrial production into human society. CSR in this regard may be defined as a socio-political effort to re-open the law's closed operative system, both cognitively and normatively.¹²⁵

V. ANALYSIS OF SYSTEM ENCROACHMENTS, CONTAMINATION, AND SYSTEM FAILURES

Applying the foregoing systems analysis to the three issues identified—labour and environment; concentrations of wealth and power; and the role of the corporation and law in society—leads to particular theorising.

First, it leads to consideration of the impact of the economic subsystem with respect to social costs. To state the obvious, it is evident that priorities within society's normative ordering or value preferences have been shifted. This shifting has impacted society, the ecology and political systems. Second, it leads to an analysis of law, which has been involved in facilitating and inhibiting various developments of and in response to those changed priorities.

¹²¹ Luhmann's curious use of language here makes sense where one thinks, as Luhmann does, about the legal subsystem's function as "not to eliminate misconceptions about what is rights because in that case any problems would be easily loved. . . The immune systems enables society to cope with the structural risk of the continuous production of conflicts." *LAW AS A SOCIAL SYSTEM*, *supra* note 66, at 477.

¹²² *Id.* at 374.

¹²³ Referred to by anthropologists as a second institutionalisation of institutionalised values. See Paul Bohannon, *The Differing Realms of the Law*, 67 *AM. ANTHROPOLOGIST* 33 (1965).

¹²⁴ See the critique of Luhmann and discussion of judges activity in SALTMAN, *supra* note 90, at 140-52.

¹²⁵ Amstutz, *supra* note 110, at 383-85; Benedict Sheehy, *Defining CSR: Problems and Solutions*, *J. BUS. ETHICS* 625 (2015).

a. Analysis of Economic Subsystem Failure and Effects

First, as to the issue of LIO's social costs or encroachment,¹²⁶ the economic subsystem has expanded and encroached on the other subsystems in a manner coincident with its own economic norms.¹²⁷ The economic subsystem's encroachment on or failure to remain within its functional domain with respect to the overall social system—as can be seen in the rising inequality in society¹²⁸, which in turn has resulted in society's inability to balance economic and ecological considerations with the consequent harm to the ecological system. The benefits are not shared equally and the costs are visited disproportionately on those with less.

The economic subsystem's encroachment has shifted preferences in value structures within the social system, which can be readily illustrated with four examples: 1) favouring the present over the future contrary to the *grund norm* of securing future life; 2) evaluating social status on the basis of wealth and consumption rather than relationships or accomplishments of other sorts; 3) preferring work as opposed to leisure; and 4) fostering social disintegration by commoditising services previously produced on the basis of kinship and community.

As to the second area of contest, the concentrations of wealth and power, they are the political consequences of economic power. They are the result of political decisions. As the political subsystem legislated and so institutionalised the grant of rights to owners of assets, it systemically dis-embedded economic production. This dis-embedding allowed a normative re-arrangement, which prioritises the increase of capital over both production and distribution of goods and services and devalued the equitable distribution of those goods and services. Further, it allowed the concentration of production and wealth generated. From a systems perspective, this dis-embedding facilitates the encroachment by the economic subsystem on the political system and destabilises the social system. This disturbance is exemplified in the business pressure on government to dismantle the welfare state. While the welfare state was largely beneficial for human functioning by prioritising human development, it was detrimental for business in that it limited opportunity to expand markets and profit. It had in-built

¹²⁶ Luhmann does not see it as encroachment. Rather, each system, as a self-referential, differentiated system, the logic of which comes from within its self-reproductive and reflective powers, interacts with its environment, and maintains only its own boundaries set to exclude and protect itself as a differentiated subsystem from the whole and adjacent subsystems. *Law and Social Theory*, *supra* note 75.

¹²⁷ And Luhmann would argue, expansionist tendencies of all systems. *See id.*

¹²⁸ Societies on the whole function better with less inequality than more. ROBERT D PUTNAM et al., *MAKING DEMOCRACY WORK: CIVIC TRADITIONS IN MODERN ITALY* (Princeton University Press 1994). While there are several expressions of inequality, the concern here is with growing economic inequality where societies are governed under neoliberal policies. *See* UNRISD, *Combating Poverty and Inequality: Structural Change, Social Policy and Politics* (2010).

limitations on profit-making opportunities by deeming more areas public so strengthening labour's hand.

b. Analysis of Legal Subsystem

These encroachments, undertaken by the economic subsystem's main actor LIO, have been facilitated by the regulatory subsystem—in this case the public legal subsystem—in various ways. It has been facilitated doctrinally by its treatment of the corporation as if it were a human person within the legal system. The courts have stated that the corporation is a person,¹²⁹ but rejected any argument that the legal person is different from the human person, a person in the liberal philosophical tradition understood to be an autonomous, rational individual—who it must be remembered—inexplicably follows social mores.¹³⁰

It has further facilitated these encroachments by adopting a procedure, which does not monitor LIOs but, as is more appropriate between liberal philosophy's human persons, is driven instead by complaints. As a result, it catches only random violations in which harmed parties have the knowledge, power, and resources to litigate. In those instances where LIO is monitored, it has been prosecuted only where public regulators have been able to catch and been adequately resourced to prosecute violators.¹³¹

These two systemic failures, social and economic, are exacerbated by developments in corporate law. Particular features of the corporation, such as limited liability and the corporate veil, encourage imposition of social costs. Further, the corporation acts a vehicle for the concentration of wealth and power. Essentially, it allows concentrated privatisation of the wealth and the externalisation of social costs.¹³² Where the corporation is used by LIO, it facilitates encroaching by the following doctrines: the doctrine of limited liability, the independent identity of the corporation, and the invention of the legal and social role of corporate director. In particular, the political decision to create the role of company director along the lines of the law of agency, rather than acting in a personal capacity, reduced the role of social inhibitions, which otherwise may have placed some constraints on economic prioritising in directors' decision-making in instances where it is clearly contrary to social and ecological public interests.

¹²⁹ *Santa Clara Cnty. v. S. Pac. R.R. Co.*, 118 U.S. 394 (1886); *Salomon v. A. Salomon & Co. Ltd.* (1897) A.C. 22.

¹³⁰ Benedict Sheehy, *Corporations and Lateral Obligations of the Social Contract*, 8 NEWCASTLE L. REV. (2004-2005). A lot of corporate law research pathologises the corporations as a "psychopath" because of its explicit rejection of such mores. JOEL BAKAN, *THE CORPORATION: THE PATHOLOGICAL PURSUIT OF PROFIT AND POWER* (Simon and Schuster 2004).

¹³¹ See JAMES MACEY, *CORPORATE GOVERNANCE: PROMISES KEPT, PROMISES BROKEN* 105-17 (Princeton University Press 2008).

¹³² *Wal-Mart*, *supra* note 7.

c. Analysis of Corporate Law and Law Reform

The third area of contest, legal control and regulation of the LIO internally through corporate law and its reform and externally through the coordination of tort, contract, and property law,¹³³ has been driven to the fore by the political decisions that allowed encroaching social costs to escalate in terms of both ecological harms and social inequality.¹³⁴ Over the century and a half since the corporate law institutionalised both limited liability and company directors as impersonal agents, it has continued to facilitate the decisions of controllers of legal corporations to prioritise private wealth generation and concentration¹³⁵—a matter begun with the invention of capitalism and as noted with the enclosure acts of the 17th century.¹³⁶ These latter acts (the doctrines of property, contract, and tort, and the legislation in these areas where touching upon the LIOs) largely favoured the wealthy who were seeking to increase control of resources and power. This class favouritism not only facilitated the development and expansion of the economic subsystem, but set the path for its encroachment on other subsystems. The groups benefiting from the encroachment for the most part did little to change the law.

Efforts to reform the law in these areas have been slow and met with only limited success. The legal subsystem has only reluctantly and slowly adapted to the social changes resulting from the developments in the economic subsystem, but did so on its function norm of equity, as illustrated by the amelioration of such laws as the *Master and Servant Act* 1823, which initially made a servant's disobedience a criminal offence,¹³⁷ the slow and protracted road to landmark cases in worker injury,¹³⁸ worker unions,¹³⁹ and product liability and eventually legislation.¹⁴⁰ Even today, in less developed countries, the difficulty in getting

¹³³ Well explained in SOULE, *supra* note 5, at 10, 17.

¹³⁴ MARTIN GILENS, *AFFLUENCE & INFLUENCE: ECONOMIC INEQUALITY AND POLITICAL POWER IN AMERICA* (Princeton University Press 2012).

¹³⁵ See Benedict Sheehy & Donald P Feaver, *Anglo-American Directors' Legal Duties and CSR: Prohibited, Permitted, or Prescribed?*, 37 DALHOUSIE L.J. (2014); see also MORTON J. HORWITZ, *THE TRANSFORMATION OF AMERICAN LAW 1780-1860*, 109-13 (Harvard University Press 1977).

¹³⁶ See, e.g., The Enclosure Act 1773 (13 Geo.3 c.81), followed by several more, and see discussion in J.L. HAMMOND & BARBARA HAMMOND, *THE RISE OF MODERN INDUSTRY* (Harcourt, Brace and Co. 1926).

¹³⁷ DOUGLAS HAY & PAUL CRAVEN, *MASTERS, SERVANTS, AND MAGISTRATES IN BRITAIN AND THE EMPIRE, 1562-1955* (University of North Carolina Press 2004).

¹³⁸ Lawrence M. Friedman & Jack Ladinsky, *Social Change and the Law of Industrial Accidents*, 67 COLUM. L. REV. 50 (1967).

¹³⁹ CHRISTOPHER FRANK, *MASTER AND SERVANT LAW: CHARTISTS, TRADE UNIONS, RADICAL LAWYERS AND THE MAGISTRACY IN ENGLAND 1840-1865*, 235-46 (Ashgate Publishing 2010).

¹⁴⁰ See ALLAN C. HUTCHINSON, *EVOLUTION AND THE COMMON LAW* (Cambridge University Press 2005).

LIOs to collaborate with governments to address the same basic issues is problematic.¹⁴¹

While at times landmark decisions by the courts have intervened to overturn these decisions of political economy—discussed in the legal literature optimistically as the “evolution of law”—the courts, for the most part, have not been a progressive force.¹⁴² Hutchinson observes that these landmark cases achieve their status because among other things, are decidedly against the legal trend. The normal course, Hutchinson writes, is “giving priority to institutional stability [i.e. the status quo] over individualised justice or wholesale reform.”¹⁴³ Hutchinson makes clear just how this normal or preferred approach amounts to the exercise of fundamentally political power and he points out that a legal subsystem focused on the integration of the economic subsystem with the social system would not have held such cases to be remarkable or landmark, and indeed would simply have gone in that direction as a matter of pursuing the course of justice—i.e. a broad approach to social fairness.

It is uncontroversial to observe that the public legal subsystem, as the institutionalisation of political decisions, is the product of the political subsystem. As demonstrated, the political subsystem has been encroached upon by the economic subsystem as governments have given way to business.¹⁴⁴ Thus in sum, from a systems perspective, it is clear that law has followed private interests of those seeking to privatise benefits while externalising social costs. It has done so through evolving corporate law doctrines.

What is evident from this discussion is that the legal subsystem failed to uphold public expectations, failed to regulate effectively, and in doing so, has failed to mitigate the social and environmental impacts of changes to business practices on a society dependent upon the ecological system. Instead, it has acted as an expression of the interests of the elite. To some extent, therefore, the problem of the regulation of the LIO is correctly characterised as a failure of the public legal subsystem to operate as the regulator of the overall social system.

That is, rather than acting as the social system’s self-reflective dimension, which it may have operated as if looked at from a Luhmann’s perspective, constraining the various subsystems to ensure the social system’s overall performance is maintained by maintaining the balance of subsystems, the legal subsystem acted to help free the economic subsystem. It did so both by its innovations in corporate law, and by normative and risk shifting in contract, property, and tort law so as to preference those with power and financial wealth

¹⁴¹ UNRISD, *supra* note 128, at §3, ch. 9.

¹⁴² GERALD N. ROSENBERG, *THE HOLLOW HOPE: CAN COURTS BRING ABOUT SOCIAL CHANGE?* (University of Chicago Press 1991). Within the law, the evolutionary theory has been critically reviewed by Hutchinson. See HUTCHINSON, *supra* note 140, at 23-56.

¹⁴³ HUTCHINSON, *supra* note 140, at 157.

¹⁴⁴ UNRISD, *supra* note 128, at ch. 2.

(as opposed to social or other types of wealth), and increasingly, allowing financial wealth to be the measure of all things.

If one is to consider a regulatory subsystem as distinct from Luhmann's autopoietic legal system, a different approach needs to be taken. That approach is turned to next. The section that follows examines regulatory systems as systems within their own right, which exert energy and force within a system, and where consciously designed as such in social systems, having specific identifiable features.

VI. REGULATORY SYSTEMS: PUBLIC AND PRIVATE

Regulation is a control activity focused on human behaviour housed in a system.¹⁴⁵ In simplest terms, regulatory systems have three elements—a tripartite construction. These are: a series of processes, infrastructure, and motivating energy discussed next.

First, the system requires the following **processes**: norm generation, a consensus on objectives, and then a decision about techniques. Moreover, some type of evaluation process will be built in so that those generating the norms can inquire whether the techniques have been successful in achieving the objectives.¹⁴⁶

Second, regulatory systems also require some **components**, usually some type of organised management of the processes just identified. Normally, the tasks will include rule making, execution, and adjudication. This institutional infrastructure in terms of public regulation may include anything from Congress or Parliaments, to agencies, to a law reform process.¹⁴⁷

Finally, regulatory systems need to be **energised** to motivate the desired behaviour. It motivates the regulatory system by use of public resources such as threats of punishment or incentives such as tax breaks, to cause people to behave in the desired ways.¹⁴⁸ In terms of private regulation, although the processes and structure of regulatory systems remains the same, the infrastructure must be privately provided.¹⁴⁹ Accordingly, it may be comprised of an organisation, such as a non-profit organisation, or a non-partisan think tank, or an industry association, usually a set of codified rules, and some type of feedback mechanism, whether through conferences, meetings, or some other form of

¹⁴⁵ *A Normative Theory*, *supra* note 18, at 395.

¹⁴⁶ *A Positive Theory*, *supra* note 30, at 988.

¹⁴⁷ Marc Schneiberg & Tim Bartley, *Organizations, Regulation, and Economic Behavior: Regulatory Dynamics and Forms from the Nineteenth to Twenty-First Century*, 40 ANN. REV. L. & SOC. SCI. 31 (2008); *A Normative Theory*, *supra* note 18, at 404.

¹⁴⁸ *A Normative Theory*, *supra* note 18, at 422.

¹⁴⁹ Benedict Sheehy, *Understanding CSR: An Empirical Study of Private Self-Regulation*, 38 MONASH U. L. REV. 103 (2012).

feedback which feeds into a consensus generation on whether objectives have been achieved with consequences with respect to system maintenance or reform. Lastly, private regulatory systems need to be motivated. They can be motivated by use of private resources from prizes, to acknowledgement, or economic incentives.

Conflicting regulatory systems exist. Regulatory systems, as noted, evaluate and restrain control inputs, throughputs, and outputs, prevent systems from explosion and implosion, and control the border between a system and its environment. This ensures adequate transfers for sustaining the system, while preventing it from being overrun. Where regulatory systems overlap, they may be in a symbiotic relationship or in conflict.¹⁵⁰ Where and to the extent that they are in conflict, the conflicts will generate a form of social friction which will appear intractable particularly as the functions, and hence, the normative foundations of the systems, are incommensurate.¹⁵¹ Such conflicts may be within a public system, as found in agencies with conflicting mandates, such as between agencies tasked with regulating environmental protection and agencies regulating promoting economic development, between public authorities as between national and subnational bodies, or between nation states in the international arena. However, conflicts may also occur between private and public regulators. While some of these conflicts have been addressed through traditional areas of law, such as conflict of laws,¹⁵² a newer approach that acknowledges and allows simultaneous, conflicting claims to juridical sovereignty, exists. This approach, called legal pluralism, accepts the simultaneous existence of different and indeed divergent regulatory authorities, jurisdictions, and issues.¹⁵³ In the current context, this approach does not place CSR and public law onto a collision course—although some argue that CSR may be viewed as an effort to displace

¹⁵⁰ Sheehy, *supra* note 34. In the policy context, this is referred to as “whole of government” policy initiatives.

¹⁵¹ These systems, says Luhmann, are “auto-poetic” or self-creating, closed systems that interact with their environment, which includes other systems. Each system’s rationality or logic is self-generated, self-referential not derived from its connection to other natural or social phenomena or environment. In one reading of Luhmann’s systems analysis, there is no politics, no overarching regulatory body, simply blind, impersonal systems which both self-create and self-regulate. But in this reading, Luhmann’s model is reductionist and naïve. *Law and Social Theory*, *supra* note 75.

¹⁵² The modern work which initially shaped the area is JOSEPH STORY, COMMENTARIES ON THE CONFLICT OF LAWS, FOREIGN AND DOMESTIC: IN REGARD TO CONTRACTS, RIGHTS AND REMEDIES (Hilliard, Gray and Co., 2nd 1841 ed. 1834). For a contemporary review, see Paul S. Berman, *Towards a Cosmopolitan Vision of Conflict of Laws: Redefining Governmental Interests in a Global Era*, 153 U. PA. L. REV. 1819 (2005).

¹⁵³ BONAVENTURA DE SOUSA SANTOS, TOWARD A NEW LEGAL COMMON SENSE: LAW, GLOBALIZATION, AND EMANCIPATION 185 (2002).

the state.¹⁵⁴ Rather, it allows both the public subsystem and the private subsystem of CSR to co-exist, cooperate, and compete.¹⁵⁵

Frictions and conflicts may frustrate the regulatory efforts as energy is diverted from regulatory objectives to maintaining the regulatory systems' space,¹⁵⁶ rather than using such energy to achieve regulatory objectives, which fall by the wayside. Such frictions and conflicts are more readily apparent at the macro level. For example, one may consider conflicts between political regulatory systems: such as the monarchical or dictatorial versus democratic, or in religion: as between competing monotheisms; and competing economic subsystems: as between pure capitalism and pure communism. These subsystem conflicts illustrate the diversion of resources away from regulatory objective of political power, one particular religion or wealth creation to subsystem space maintenance. Yet at a subsystem level, the frictions and conflicts, while not as obvious, can pose equally apparently intractable problems. So, at the interface of largely private economic and public legal subsystems, the competition to regulate the corporation and the LIO it houses provides for frictions as well as symbiosis.

As Teubner observes, subsystems such as law may damage neighbouring subsystems by over-legalising them.¹⁵⁷ We may extrapolate from this observation to describe the economic as “over-economising” its neighbours, and in this context of increasingly independent economic subsystems, Teubner describes “the task of juridification . . . to bring the rationality of other social subsystems into play against the economy.”¹⁵⁸

How then is one to accomplish this task of pushing back on the economic subsystem? How do we control LIO and its harms? One must resort to private regulation through social activism¹⁵⁹ or CSR.¹⁶⁰ In this regard, Teubner observed “CSR represents a contradiction between guiding principles of the political subsystem and the economic subsystem” and amounts to a “politicization of the economy”¹⁶¹ –perhaps more accurately a second politicisation.¹⁶² Taking this view of CSR, the analysis may be construed as a contest and a collaboration

¹⁵⁴ Noted in Crouch, *supra* note 59, at 41.

¹⁵⁵ M. Herberg, *Global Legal Pluralism and Interlegality: Environmental Self-Regulation in Multinational Enterprises as Global Law-Making*, in RESPONSIBLE BUSINESS: SELF-GOVERNANCE AND LAW IN TRANSNATIONAL ECONOMIC TRANSACTIONS 262 (O. Dilling et al., eds., 2008).

¹⁵⁶ *Law and Social Theory*, *supra* note 75, at 181.

¹⁵⁷ TEUBNER, *supra* note 33, at 22-27.

¹⁵⁸ *Id.* at 32.

¹⁵⁹ SOULE, *supra* note 5.

¹⁶⁰ See, e.g., *id.* Not all commentators are as hopeful about the utility of litigation in leading law reform. For this contrary view, see, e.g., ROSENBERG, *supra* note 142.

¹⁶¹ Teubner, *supra* note 77, at 160.

¹⁶² Guido Palazzo & Andreas Scherer, *Corporate Social Responsibility, Democracy, And The Politicization Of The Corporation*, 33 ACAD. MGMT. REV. 773 (2008).

between private economic and public legal subsystems operating as regulatory systems seeking to control LIO pursuing different but related norms.

The next section, therefore, examines CSR as a form of regulation, private regulation, aimed at regulating LIO.

VII. CSR AS PRIVATE LAW IN SYSTEMS PERSPECTIVE

Changes in subsystems and their boundaries have reshaped the state¹⁶³ and created a space which has permitted private regulatory regimes to increase in scope of activity, jurisdiction, and in sophistication, while simultaneously shifting, displacing, and at times, undermining the position of the state as the exclusive centre of authoritative regulation.¹⁶⁴ One explanation of these changes, including the displacement of government from its role as the sole authoritative source of regulation, from a systems perspective, is that the newer private system and transformed regulatory state result from the increasing specialisation, differentiation, and disintegration of increasingly complex social systems. Teubner suggests that this fragmentation of systems gives rise to CSR in the first instance.¹⁶⁵ Teubner wrote: “CSR can be understood only in terms of differentiation and integration of society.”¹⁶⁶ The increased specialisation and shift of the economic subsystem from provisioning the current generation and saving for the future to wealth creation has both required and served to disconnect the economic subsystem from the broader social system. This logic led Teubner to a critical insight, namely,

“CSR serves as one among several integrative devices in society which is characterised by extreme functional differentiation. . . [answering] The most conspicuous trait of the process of differentiation. . . the high degree of autonomy attained by the economic subsystem.”¹⁶⁷

Teubner’s analysis, however, does not go far enough. It explains neither how it does so, nor the process by which it occurs—something this paper argues occurs by way of regulation. Nevertheless, what Teubner’s analysis does accomplish is that it allows us to explain the economic subsystem’s social costs in a systems framework as no more than a contamination or encroachment by the economic subsystem on neighbouring subsystems and further, it allows CSR to be viewed as the economic subsystem’s self-reflective or regulatory dimension

¹⁶³ See HARVEY, *supra* note 27, at 64-81.

¹⁶⁴ See HARVEY, *supra* note 27, at 64-6; Picciotto, *supra* note 26. See generally Dilling et al., *supra* note 26.

¹⁶⁵ See Teubner, *supra* note 77, at 161-62.

¹⁶⁶ *Id.*

¹⁶⁷ *Id.* at 161.

attempting to constrain the economic subsystem itself. Before exploring this insight further, we turn to examine with greater detail both public law and private law as regulatory systems.

VIII. PUBLIC AND PRIVATE LAW

As noted, although Luhmann does not see law as a regulatory system, this paper takes the opposite view. It sees law as functioning as a significant regulator in the social system. Further, law here is seen not as unitary, but as plural in terms of sources, objectives, and resources. In this section, the tripartite framework for regulation outlined above is used.

a. Public Law as Regulation

Applying the tripartite framework for regulation, we note first the discrete **processes** of norm generation, the development of consensus on objectives and decisions about techniques in public law. Public law's norms are drawn from the political sphere. Politics, as noted, is not distant from law and nor is it distant from power—economic or otherwise. It has conflicting norms of ensuring economic provisioning of the population. On the one hand, in a capitalist economy by way of consistent economic growth, and on the other, preserving the natural environment. Further, the public politicians face the conflict of being tasked with developing policies that will maintain social stability while ensuring sufficient popularity to be re-elected. Law's own norms are inconsistent. There is a set of norms concerning the common wealth that to a considerable degree are inconsistent with norms around private rights. This is a problem of normative ordering.¹⁶⁸

As to the process of developing objectives, the public legal system has a wide range of objectives that extend well beyond the sole focus of LIO. From a systems perspective, the public legal subsystem in a social system provides stable expectations. In a democratic society, it is expected to reflect the interests of the majority—i.e. majority power. It does so through a combination of laws, such as public laws of environmental protection, administrative law, and constitutional law, and private laws such as contract, tort, and property. The law allows people to function in a way that provides a relatively predictable social existence or stable expectations¹⁶⁹ based on knowledge of who is in control, what controls they may have, what the limits of that control are—i.e. accountability, and how to protect themselves. It also allows people to arrange their affairs in ways that suit them and provides security. Finally, in a rule of law state, it limits government

¹⁶⁸ *A Normative Theory*, *supra* note 18, at 412-13.

¹⁶⁹ This view of law providing stability is consistent with Luhmann's idea that the function of law is to maintain expectations despite disappointments. *LAW AS A SOCIAL SYSTEM*, *supra* note 66, at ch. 3.

action against citizens. In these ways, law is designed to provide a significant benefit to society.

Given this broad task and wide range of objectives, it is unsurprising that with respect to matters concerning LIO, the law has dealt with them as discrete phenomena. Externalities have been assigned to distinct areas of law, namely tort, contract, environment, labour, and employment law. The law has not focused on the actor involved or particular systems as a whole. Rather, each of these areas of law deals with the specific issues and externalities starting from different principles, utilising different doctrines. Why is this the case? There is a *prima facie* case for this organisation of law—i.e. not limiting torts, contracts, etc. to the corporation or LIO. Ordinary persons regularly commit torts, breach contracts, and destroy the natural environment. There is no need to make these issues peculiarly corporate law issues. The regulatory techniques law uses is primarily damages, and in limited cases, injunctions and restitution. These techniques are embedded in substantive and procedural law.

The second part of the tripartite regulatory framework considers **components** that make up the institutional infrastructure. The well-known institutions of the three branches of government, the relevant agencies, and the civil service need no further mention other than the function just noted. Issues of efficacy and coherence are unrelated to the analysis of their role in a regulatory system.¹⁷⁰

As to the third part, energising the regulatory system through appropriate **motivation**, the public law has the widest array of potential methods. These range from the execution of public legal authority, to public economic resources to any type of license, fine, or grant imaginable. Most public regulatory systems rely on combinations of these methods, including the much-discussed “new methods” of regulation.¹⁷¹

b. Public Law and Corporations

In terms of the substantive law of corporations, law has done four things: (1) It has created the entity, (2) it has organised the corporation internally, (3) it has determined the corporation’s relationship with outside parties, and (4) it has established both the procedure and substance for contest and clash between the corporation and other members of society—they are dealt with through the legal system, as are conflicts between any other persons.

In terms of its creation, however, the corporation has a unique status in the legal subsystem.¹⁷² It is law’s unique child—it is law’s person. This peculiar status gives it full participatory rights in the legal subsystem, and of particular

¹⁷⁰ See *A Normative Theory*, *supra* note 18; *A Positive Theory*, *supra* note 30.

¹⁷¹ See *id.*; see also ROBERT BALDWIN & MARTIN CAVE, *UNDERSTANDING REGULATION: THEORY, STRATEGY, AND PRACTICE* (Oxford University Press 1999).

¹⁷² *Salomon v. A. Salomon & Co. Ltd.* (1897) AC 22, 27.

import for this paper, the economic rights of holding property¹⁷³ and entering into contracts.¹⁷⁴ Thus, it is simultaneously a legal person and a unique economic actor. All other actors in both the legal subsystem and the economic subsystem are human, and so, subject to human social inhibitions and constraints. By way of contrast, the legal corporation is wholly disembodied.¹⁷⁵ As such, it is the truly atomised individual of neoclassical economics—advancing primarily economic interest.¹⁷⁶

As this lego-economic actor is not subject to social inhibitions, indeed, it has been described as “psychopathic”¹⁷⁷ and indeed “criminal”¹⁷⁸ because it pursues the powerful new norm of wealth accumulation, particularly as taken up by the powerful elite leaders following their own elite consensus on norms and values.¹⁷⁹ Further, this lego-economic actor’s internal workings are not subject to democratic control. People whose lives it controls, i.e. its workers, and people’s lives it affects, i.e. the community, have no rights in its internal governance. Rather, those rights are distributed to directors and officers on the basis of private politics among incorporators. It is established and organised based on private economic interests and so is not accountable to the public. Indeed, it has been argued that the corporation is unique among legal concepts and doctrines in that it is the only aspect of the legal subsystem not set up in principle to benefit society.¹⁸⁰ Thus, although the right to incorporate is a publicly granted right, the corporation itself is considered a private matter. As a private matter, it is not subject to the public scrutiny and accountability as it would be if it were public, and no account, hence is required, regardless of the quantity of power or resources under its control.

The relations it has with insiders or outsiders are thus not a function, which is dependent upon its power. Rather, as determined by law, these are all private matters settled as between the incorporators as they choose to distribute rights and duties among themselves. The issue of relations with outsiders requires further consideration, however, in thinking about the topic of this paper, namely, social costs.

¹⁷³ *Bowman v. Secular Society Ltd.*, A.C. 406, 440-41 (1917).

¹⁷⁴ *Defell v. White*, L.R.2, C.P. 144 (1866).

¹⁷⁵ Sheehy, *supra* note 130. The matter of embeddedness is discussed in Granovetter, *supra* note 70.

¹⁷⁶ The theoretical economic norm of shareholder primacy does not translate well into social reality. MARSHALL M. MEYER & LYNNE G. ZUCKER, *PERMANENTLY FAILING ORGANIZATIONS* (SAGE Publications 1989).

¹⁷⁷ See BAKAN, *supra* note 130.

¹⁷⁸ STEVE TOMBS & DAVID WHYTE, *THE CORPORATE CRIMINAL: WHY CORPORATIONS MUST BE ABOLISHED*, KEY IDEAS IN CRIMINOLOGY SERIES (Routledge 2015).

¹⁷⁹ See CHARLES MILLS WRIGHT, *THE POWER ELITE* (Oxford University Press 1956); Granovetter, *supra* note 70.

¹⁸⁰ See GREENFIELD, *supra* note 16.

Finally, in terms of procedure, law has set the corporation's activities as to be controlled as any other human persons. It is to be left alone, prosecuted after the fact on an ad hoc basis for breaches of the social norms. Of course, this greatly reduces the number and types of actions, which will be brought, particularly in the case of LIO. Only those with the time, money, and inclination to challenge a LIO will put themselves into such situations. LIOs are well known to abuse the legal subsystem through SLAPP suits,¹⁸¹ using their disproportionate resources to silence those who would challenge their operations.¹⁸² In addition, there are administrative agencies, which can bring actions against members of the public for breach of state laws such as environmental harms. The efficacy of such agencies, however, is questionable as they are often not only chronically underfunded,¹⁸³ but subject to political whim¹⁸⁴ and may suffer such poor regulatory coherence as to result in regulatory failure.¹⁸⁵ Given this complaint driven approach and the potential economic benefits of ignoring both law social inhibition, it is hardly surprising that there would be a considerable gap between public expectations of law's ability to reign in the corporate economic actor, and its actual ability to do so.

c. CSR as Regulation

Applying the tripartite framework of regulatory systems to CSR, it can be noted that CSR involves the three normal regulatory **processes** of norm generation, consensus on objectives, and a decision about techniques. First, in terms of norms, it presents somewhat of an unresolved conflict: as noted, Teubner observed, "CSR represents a contradiction between guiding principles of the political subsystem and the economic subsystem" and amounts to a "politicization of the economy."¹⁸⁶ The norms, however, are not so much in conflict—all parties agree that the ecology is important and that a sustainable economy, where "economy" means providing for human sustenance, is necessary. The disagreement is more about the prioritisation of the norms—a political matter.¹⁸⁷ CSR, with its roots in private economics and private rights, prioritises by default, such rights. Where the focus is on public rights or the public commons, it struggles at its core. Yet, this conflict or disagreement is not the only disagreement.

¹⁸¹ George W. Pring & Penelope Canan, *An Introduction for Bench, Bar and Bystanders*, 12 U. BRIDGEPORT L. REV. (1991-1992).

¹⁸² There are many other means by which LIOs abuse the legal process.

¹⁸³ John B. Stephenson, *Chemical Regulation: Options for Enhancing the Effectiveness of the Toxic Substances Control Act*, U.S. GOV'T ACCOUNTABILITY OFFICE (2009).

¹⁸⁴ Richard N.L. Andrews, *The EPA at 40: An Historical Perspective*, 21 DUKE ENVTL. L. & POL'Y F. 223 (2011).

¹⁸⁵ *A Normative Theory*, *supra* note 18; *A Positive Theory*, *supra* note 30.

¹⁸⁶ Teubner, *supra* note 77, at 160.

¹⁸⁷ *See* Sheehy, *supra* note 125.

CSR norms are set by private interests. The lack of public input provides a basis for the concerns about private regulation's democratic deficit in which public norms are displaced and so failing to reflect democratic public interest.¹⁸⁸ Where CSR is to reach a larger group, some avenue for public input will be necessary.

Second, as a form of regulation, CSR needs a consensus of objectives.¹⁸⁹ In this area, CSR is particularly divided. The positions range from improved marketing of the LIO, known as "greenwashing",¹⁹⁰ to moderating social costs by focusing on particular LIO policies or products,¹⁹¹ to wholesale industry changes,¹⁹² to radical change to economic systems.¹⁹³

As to the third process, namely, selection of techniques, a whole range is available. First, one may consider public law—i.e. government initiated. Second, one may think of private initiatives such as ISO 26000 or SA8000. Soule classifies a third set of techniques as insider tactics and outsider tactics. In terms of insider tactics she identifies shareholder activism through use of shareholder resolutions, socially responsible investment and its related techniques of community or social investing and micro-lending, and ethical screening—negatively for objectionable LIOs or positively for desirable LIOs.¹⁹⁴ As to outsider techniques, she identifies boycotts, corporate campaigns of various types, advocacy science, tempered activism, collective legal manoeuvres, and protest demonstrations.¹⁹⁵ While arguably not all of these activities fit comfortably under the rubric of CSR where CSR is conceived as corporate

¹⁸⁸ See Kernaghan Webb & A. Morrison, *The Law and Voluntary Codes: Examining the "Tangled Web"*, in VOLUNTARY CODES: PRIVATE GOVERNANCE, THE PUBLIC INTEREST AND INNOVATION 97-104 (Kernaghan Webb ed., 2004); see also KERNAGHAN WEBB, VOLUNTARY CODES: PRIVATE GOVERNANCE, THE PUBLIC INTEREST AND INNOVATION (Carleton Research Unit for Innovation, Science and Environment, Carleton University ed., 2004); Crouch, *supra* note 59; A. Sobczak, *CSR: A New Form of Social Regulation for Labour Relations within Transnational Companies*, in THE RESPONSIBLE CORPORATION IN A GLOBAL ECONOMY (Colin Crouch & Camilla Maclean eds., 2011).

¹⁸⁹ See Sheehy, *supra* note 125.

¹⁹⁰ Stepan Wood, *Green Revolution or Greenwash? Voluntary Environmental Standards, Public Law and Private Authority in Canada*, in NEW PERSPECTIVES ON THE PUBLIC-PRIVATE DIVIDE (Law Commission of Canada ed. 2004). See discussion in Ronen Shamir, *Corporate Social Responsibility: A Case of Hegemony and Counter-Hegemony*, in LAW AND GLOBALIZATION FROM BELOW: TOWARDS A COSMOPOLITAN LEGALITY (Bonaventura De Sousa Santos & César A. Rodríguez-Garavito eds., 2005).

¹⁹¹ SOULE, *supra* note 5, at 53-86.

¹⁹² *Id.* at 104-45 provides a series of case studies dealing with efforts to change industry practices from tuna fishing to chemical production.

¹⁹³ JONATHON PORRITT, CAPITALISM: AS IF THE WORLD MATTERS (Earthscan 2005).

¹⁹⁴ SOULE, *supra* note 5, at 10-12.

¹⁹⁵ *Id.* at 12-18.

policy,¹⁹⁶ they do represent private efforts at regulating LIO behaviour. The decision to sustain, terminate, or modify regulatory efforts is dependent upon the objective,¹⁹⁷ so which an established objective one cannot identify any particular feedback system.

Second, as to the **components** of the institutional infrastructure, again, there is no single approach among CSR participants.¹⁹⁸ While a debate exists among political science scholars about the desirability and efficacy of organisation,¹⁹⁹ from a regulatory perspective, there is clear infrastructure both established which can be drawn upon, and developing which can address the issues. As examples, one may consider the private industry initiatives such as forestry industry's Forest Stewardship Council,²⁰⁰ consumer driven Fair Trade Movement,²⁰¹ the jewellery industry's Kimberley Process,²⁰² the chemical industry's Responsible Care Program,²⁰³ and on the public side the UN's GRI,²⁰⁴ all of which function as and provide regulatory infrastructure to contribute to the regulation a large number of LIOs.

Third as to the **motivation** energising the regulatory system, one can see from the above list a variety of incentives and potential punishments.²⁰⁵ The incentives include the social and economic value of certification and social acceptance or license. The punishments would include disclosure of unacceptable

¹⁹⁶ Archie B. Carroll, *Corporate Social Responsibility: Evolution of a Definitional Construct*, 38 BUS. & SOC. 268 (1999). *But see* Sheehy, *supra* note 130. While not explicitly including such activities by identifying CSR as a political movement, includes political activities of all types including demonstrations.

¹⁹⁷ See SOULE, *supra* note 5, at 29-52.

¹⁹⁸ Sheehy, *supra* note 130.

¹⁹⁹ SOULE, *supra* note 5, at 32-33.

²⁰⁰ FOREST CERTIFICATION: AN INNOVATIVE INSTRUMENT IN THE SERVICE OF SUSTAINABLE DEVELOPMENT? (Dietrich Burger et al. eds., Deutsche Gesellschaft für Technische Zusammenarbeit (GTZ) GmbH 2005); *see also* Lars H. Gulbrandsen, *Overlapping Public and Private Governance: Can Forest Certification Fill the Gaps in the Global Forest Regime?*, 4 GLOBAL ENVTL. POL. 75 (2004).

²⁰¹ See comparison of approaches in Peter Leigh Taylor, *In the Market But Not of It: Fair Trade Coffee and Forest Stewardship Council Certification as Market-Based Social Change*, 33 WORLD DEVELOPMENT 129 (2005).

²⁰² Virginia Haufler, *The Kimberley Process Certification Scheme: An Innovation in Global Governance and Conflict Prevention*, 89 J. BUS. ETHICS 403 (2009).

²⁰³ Magali A. Delmas & Ivan Montiel, *The Diffusion Of Voluntary International Management Standards: Responsible Care, ISO 9000 And ISO 14001 In The Chemical Industry* (ISBER Publications, Institute for Social, Behavioral, and Economic Research, UC Santa Barbara 2007); *see also* Andrew King & M. Lennox, *Industry Self-Regulation Without Sanctions: The Chemical Industry's Responsible Care Program*, 43 ACAD. OF MGMT. J. 698 (2000).

²⁰⁴ See Ralitzia Nikolaeva & Marta Bicho, *The Role of Institutional and Reputational Factors in the Voluntary Adoption of Corporate Social Responsibility Reporting Standards*, 39 J. ACAD. OF MARKETING SCI. 136 (2011).

²⁰⁵ Sheehy, *supra* note 149.

practices, exclusion from groups, revocation of certification, and various insider and outsider tactics. Where CSR lacks critical framework, problems emerge which are inimical and ultimately fatal to the project.²⁰⁶ Accordingly, CSR can be understood and analysed in terms of regulatory systems. The next section then examines how CSR approaches its regulatory task.

d. CSR Regulating LIO

Contrasting CSR to public law clarifies how CSR is a markedly different approach toward regulating LIO. There are three significant distinctions. In the first instance, CSR has a different starting point. This regulatory effort starts with a focus on the social and physical phenomena of social costs, on concentrations of power, and on environmental degradation, whereas public law's focus is on legal phenomena—namely, rights and duties. Secondly, CSR focuses on a specific actor, LIO and the corporation, which as noted are not distinguished in the literature.²⁰⁷ Public law focuses on rights and duties in tort, contract etc. Thirdly, in contrast to public law, which is a state based authoritative body of law, CSR is a private regulatory initiative²⁰⁸ which garners its regulatory power from non-public resources, such as consumer demand, institutional pressures and the like, all of which seek to regulate LIO's behaviour with respect to certain aspects of industrial production, including practices and some incidents of corporate law.

While business interests may define CSR as “businesses’ commitment to contribute to sustainable economic development, working with employees, their families, the local community, and society at large to improve their quality of life”,²⁰⁹ a broader scholarly definition as a field of inquiry²¹⁰ is best refined as understanding CSR as a form of international private business regulation.²¹¹ More fully, at a theoretical level I have defined CSR elsewhere as “CSR is a type of international private law and can be defined as a socio-political movement which generates private self-regulatory initiatives, incorporating public and private international law norms seeking to ameliorate and mitigate the social harms of and to promote public good by industrial organisations. . . [in short] international private business self-regulation.”²¹² Thus, in the context of this paper, CSR is

²⁰⁶ See Philipp H. Pattberg, *The Forest Stewardship Council: Risk and Potential of Private Forest Governance*, 14 J. ENVT. & DEV. 356 (2005).

²⁰⁷ *Interfaces*, *supra* note 10; but see SOULE, *supra* note 5.

²⁰⁸ Sheehy, *supra* note 149, at 104.

²⁰⁹ World Business Council for Sustainable Development, <http://www.wbcsd.org/> (last visits Feb. 17, 2017) [hereinafter WBCSD], *cited in* RONNIE V. DE CAMINO, *FOREST MANAGEMENT AND DEVELOPMENT*, (Dietrich Burger et al. eds., 2005).

²¹⁰ Andrew Crane et al., *supra* note 11. For an overall understanding of the issue, see Sheehy, *supra* note 125.

²¹¹ Sheehy, *supra* note 125.

²¹² *Id.* at 639.

an... effort to regulate the externalities, inequalities and concentrations that result from LIO and a space for political debate about regulating LIO—i.e. control of LIO. By this definition, CSR is a form of private politics.²¹³ As social phenomenon, CSR is a type of private self-regulation.²¹⁴ This understanding may be expanded further by identifying CSR as a form of regulation emanating from the economic subsystem. What makes CSR interesting from a regulatory perspective is that it can be understood as regulation generated by the economic subsystem, but with norms that run contrary to market norms—at least to some extent.²¹⁵ What it seeks to do is include public non-economic concerns within the economic subsystem which subsystem is based on prioritising private economic norms.

CSR's focus on the particular actor, the LIO, has caused CSR to be described as “new corporate law” by some scholars.²¹⁶ These scholars explain their use of the term because as they see it: “[CSR is] a system of corporate regulation that depends as much on (if not more on) non-statutory mechanisms and methods, which in many cases can have a more immediate impact on corporate operations.”²¹⁷ This position is significant because the corporation that houses the LIO is a creature of the nation state and subject to the local laws. It is at this national level that corporate law operates and the specifics of corporate regulation are worked out. Accordingly, it is at the level of the nation state that CSR may be seen as a competing or complementary regulatory regime.

CSR also functions as a form of regulation in the international sphere. Sahlin-Andersson's institutional analysis provides a useful insight.²¹⁸ Essentially, she argues that CSR functions as a members' club in which prestige serves to keep up membership. She argues that little more than mere membership is required and for the most part, little more given—although some argue that as private politics, it has considerable effect.²¹⁹ CSR as a soft norm may be more important in the international reach of MNCs.²²⁰

²¹³ See SOULE, *supra* note 5, at 31-5.

²¹⁴ Sheehy, *supra* note 125.

²¹⁵ Susan Hart, *Self-Regulation, Corporate Social Responsibility, and the Business Case: Do They Work in Achieving Workplace Equality and Safety?*, 92 J. BUS. ETHICS 585 (2010). (there is, of course, a whole literature on the business case for CSR, not to mention the many non-market actors involved).

²¹⁶ Stephen Bottomley & Anthony Forsyth, *The New Corporate Law: Corporate Social Responsibility and Employees' Interests*, in *THE NEW CORPORATE ACCOUNTABILITY: CORPORATE SOCIAL RESPONSIBILITY AND THE LAW* (D. McBarnet et al. eds., 2007).

²¹⁷ *Id.* at 64

²¹⁸ Kerstin Sahlin-Andersson, *Corporate Social Responsibility: A Trend and a Movement, but of What and For What?*, 6 CORP. GOVERNANCE 595 (2006).

²¹⁹ SOULE, *supra* note 5, at 154-5.

²²⁰ Robert B. Thompson, *Globally Integrated Corporations as “Good for the Country”*: *The Impact of Soft Law* 16-7 (Vanderbilt Pub. L. Research Paper No. 08-35); David Crowther & Nicholas Capaldi, *Introduction: An Agenda for Research* to DAVID CROWTHER & NICHOLAS

CSR as regulation is more than the institutional pressures of club membership. It is clear from an examination of the legal regulatory literature that CSR is a form of regulation using two well-recognised techniques: regulation by information and regulation by incentives.²²¹ Regulation by information is well known in the corporate world by certifications and from the disclosure requirements placed on companies listed on public stock exchanges. Certifications are public representations of achievement, usually conferred or verified by third parties.²²² The mandatory disclosure regimes force corporations to disclose their financial positions and to report them in a certain, certified format. By doing so, these certification and disclosure regulatory regime places corporations that do not comply, or that fail to achieve adequate returns at risk of a change of management or takeover.

The disclosure regime therefore causes LIO corporations to conduct their affairs in certain preordained ways. Public, independently verified information that is complied and presented in a way that makes it possible to compare competitors enhances the regulatory potential of the information. In this context, certification becomes increasingly important.

In the context of CSR, disclosure can occur voluntarily or involuntarily. In an involuntary disclosure, where NGOs disclose LIO environmental impacts or political activities, the revelation of information operates in much the same way as voluntary regulation by information. LIO's voluntary engagement in activities such as Triple Bottom Line²²³ reporting and the GRI,²²⁴ is CSR regulation by information.

CSR also regulates using another well-known technique of incentives, a form of regulation by market.²²⁵ Where a LIO is failing to act in ways deemed appropriate by communities, those communities may organise economic penalties such as boycotts. Again, management response to or anticipation of such economic threats maybe considered either internal or external, but in either case, are a form of regulation by CSR. These two regulatory techniques, however, demonstrate that the normative ordering of private regulation prioritises economic profit seeking norms above all others and so constrains the regulatory systems ability to constrain the economic subsystem and LIO.

CAPALDI, THE ASHGATE RESEARCH COMPANION TO CORPORATE SOCIAL RESPONSIBILITY 12 (David Crowther & Nicholas Capaldi eds., 2008).

²²¹ See, e.g., OGUS, *supra* note 171, at 41, 49.

²²² The value in CSR certification as a market signalling technique is an emerging area of research. See Thomas Lys et al., *Signaling Through Corporate Accountability Reporting*, 60 J. ACCT. & ECON. 56 (2015).

²²³ JOHN ELKINGTON, CANNIBALS WITH FORKS: THE TRIPLE BOTTOM LINE OF 21ST CENTURY BUSINESS (Capstone 1997).

²²⁴ See Nikolaeva & Bicho, *supra* note 204.

²²⁵ OGUS, *supra* note 171, at 18-22.

CSR seeks to regulate in two other important dimensions. First, at the local level, business needs a social license to carry on its productive, profit-generating activities.²²⁶ These activities require acceptance by the local community to avoid civil unrest or direct action against the business organisation via attacks on its property or employees.²²⁷ This dimension is addressed through adequate wages, acceptable environmental and social impacts as measured at the local level by local standards and may include philanthropy. This aspect of regulation is the LIO's outwardly directed regulation—regulating the community response in which it operates. This regulatory effort is increasingly important in a globalised world as the community increasingly includes consumers in other countries as Nike, Apple and other companies have discovered.

The second dimension of CSR as regulation is markedly as subtle as it is important. CSR is mostly a matter of concern about regulating LIOs, including MNCs that have the resources of many smaller countries and produce negative externalities of global proportions. It is evident that LIOs seek to regulate potential organised opposition. This regulation requires a strategic response to potential trouble for LIO's profit-making abilities and may lead to greenwash or genuine and truly transformative CSR.

LIO, although purporting to serve the public, does not allow the public into its decision-making, to access its information about its impact, nor to consult the public on its policies. Rather, it sets its priorities and develops its policies to coincide with its private economic norms, and the personal political norms and priorities of the elites in control.²²⁸ This lack of democratic input keeps the main two issues from the policy discussion: the reduction of material consumption to allow humans to live within the ecological boundaries of the planet,²²⁹ and leaving democracy to the voters.²³⁰

With this review of the two regulatory systems, public law and private CSR, the discussion now turns to review how the two regulatory systems approach the three externalities.

²²⁶ This argument is based on the literature on corporate citizenship and license. See, e.g., Jennifer Howard-Grenville et al., *Constructing the License to Operate: Internal Factors and Their Influence on Corporate Environmental Decisions*, 30 L. & POL'Y 73 (2008). See also Sheehy, *supra* note 149.

²²⁷ SOULE, *supra* note 5, at 53-80.

²²⁸ Vitali et al., *supra* note 71. Rupert Murdoch, for example, was recently criticised at the Annual General Meeting of the shareholders of News Corp for use of corporate funds to achieve his personal political views but ignored the criticism. Benedict Sheehy, *For News Shareholders, It's Rupert's Way or the Highway*, THE CONVERSATION (Oct. 22, 2012), <https://theconversation.com/for-news-shareholders-its-ruperts-way-or-the-highway-10231>.

²²⁹ Peter Newell, *CSR and the Limits of Capital*, 39 DEV. & CHANGE 1063 (2008).

²³⁰ Overton, *supra* note 56; NOREENA HERTZ, *THE SILENT TAKEOVER: GLOBAL CAPITALISM AND THE DEATH OF DEMOCRACY* (Arrow Books 2001).

IX. REGULATING LIO, REGULATING THE CORPORATION

LIO and its three externalities—social costs, concentrations of wealth and power, and corporate law—are addressed, at least nominally, through a contest over the corporation. The contest between public law and private CSR occurs at three critical points: 1) distributions benefits and costs (and in particular social costs), 2) the right to make purposive and distributive decisions and 3) the proper construal of the industrial organisation itself. Each of these contests are essentially about how to characterise the LIO and where to draw its boundaries—i.e. to decide who are insiders and have their values implemented and who will be external to the LIO and can be ignored.

a. Social Costs

Social costs are the main concern addressed by CSR regulation. These costs may be understood systemically as resulting from the economic subsystem's encroachment on neighbouring subsystems. It fails to act self-reflectively so that it may be evaluative of its performance and restrain its activity to avoid undermining the differentiated, neighbouring specialised subsystems.

CSR views externalities as issues belonging to LIO and which ought to be the subject of internal corporate regulation only. Rather than looking to public regulatory responses, CSR advocates suggest that these are best addressed via insiders making “better” decisions. Of course, “better” decisions are a normative category, subject to political settlement as well ethical argument. And this leads back to the fundamental questions: who is to benefit from the LIO? Who is to bear its costs? And, how and on what basis are these decisions to be made? Yet, as has been noted, corporate law has already set its limits and focus. And further, public law has determined that these costs will be addressed on an ad-hoc, post facto basis.

Yet some CSR advocates suggest that these externalities should be internalised by LIO and some reform is called for to ensure they become essential aspects of corporate law. These advocates see a solution in expanding the law of corporations to encompass all the productive activities (as opposed to merely the internal legal arrangements) and by expanding, catching, and internalising the external consequences of LIOs productive activities. In this view, corporate law is not merely insiders concerns expressed in terms of corporate rights and duties. In this vision, corporate law would regulate the rights and duties of employees, restrict the nature and type of industrial activities carried on by the corporation, including potentially industrial processes, so as to limit environmental consequences, and take account of other unspecified community concerns. The pressure to internalise social costs is applied, as noted, by a combination of insider and outsider tactics.

Traditional corporate law scholars and generally those favouring the status quo oppose any such re-arranging, refocusing on inclusion of non-financial considerations into corporate law. In this approach to corporate law, social costs are trivialised, excluded from the legal analysis and relegated to other areas of law which so as to favour wealth generation as opposed to efficient production and distribution. The extent to which LIO is expected to deal with social costs in this latter paradigm is essentially a type of cost-benefit-analysis, another efficient breach, in this case, of the social contract.²³¹

b. Concentration of Decision-Making and LIO as Political Actor

The area of corporate decision-making is hotly contested as it is obvious that whoever participates in decision-making has power to regulate the corporation, and hence LIO along with his/her own normative lines toward his/her preferred ends. Whereas corporate law has clearly established decision-making structures and processes, at least since the early 20th century, CSR views it as wide open.²³² As such CSR is an area of interest for scholars involved in the corporate governance debate. The “who” and “for what ends” debates about corporate activity have resurrected the political discussion.

The basic argument is that a LIO with a social footprint equal to that of governments of many nation-states should, like government, have its decision-making processes and decisions open to scrutiny by parties affected by those decisions, if not subject equal input. In other words, the expanded role, rights and benefits granted to LIO exploiting the corporate form in an industrial society normatively should²³³ carry an equally expanded duty with respect to the protection and maintenance of that society. A corollary of this proposition is that those regulating the LIO - the corporate controllers, the directors, and officers - will not only have greater responsibilities, but will also need expanded discretions to address these responsibilities, a matter which leads to consideration of the debate that has run at least since Berle and Dodd in the 1920s.²³⁴

Both were concerned about the LIO’s corporation in the America of their day. They noted the great power and wealth amassed by these corporations. They also noted the great impacts of corporate activity on society. Finally, they worried about the power of directors who controlled the corporations. Berle focused more

²³¹ Sheehy, *supra* note 130.

²³² Amstutz notes that this issue lies behind the EU’s decision to exclude non-industrialists from its CSR dialogue. Amstutz, *supra* note 110.

²³³ This proposition seems to cause consternation for some scholars who appear to be market fundamentalists, to use Stiglitz’s term, or who have misunderstood Hume’s attack on St. Anselm’s ontological argument. Gordon Smith, *Wal-Mart’s Irresponsible Pickle Strategy*, CONGOLMERATE (Dec. 29, 2006), http://www.theconglomerate.org/2006/12/walmarts_irresp.html#comments.

²³⁴ A.A. Jr Sommer, *Whom Should the Corporation Serve—The Berle-Dodd Debate Revisited Sixty Years Later*, 16 DEL. J. CORP. L. 33 (1991).

narrowly on the power of directors and managers in the exercise of their discretion over the vast assets of the corporate empires, and the potential use of those powers to divert corporate power and assets to serve the directors' own personal ends. Berle expressed it as a concern that the parties whose money these managers were dealing with had little control over those managers—an issue he identified along with Gardiner Means as the separation of ownership and control.²³⁵ Berle's proposition for reigning in directors and protecting investors was to make directors accountable to shareholders. His view was one shared by others from the same era and has become the basis for the economic orthodoxy of shareholder primacy.²³⁶

Dodd focused on the broader issue of political power of large corporate empires referred to here as LIOs.²³⁷ He argued that corporate law should “protect the nation from corporations”²³⁸ – i.e. protect society from LIO's social footprint or regulation of society by LIO as robber baron industrialists did during the early industrial revolution.²³⁹

Dodd, like Berle, focused on directors' duties. However, his view was that shareholders were not uniquely vulnerable to corporate exploitation. He suggested that the directors of corporations take account of social needs, and according to Chen and Hanson, saw the separation of ownership and control as an opportunity to exploit corporate wealth for the betterment of society.²⁴⁰ This view gave rise to the “director-statesman model” popular in the mid-twentieth century.²⁴¹

These views have been advanced over the intervening decades by a variety of actors, and most recently have been advanced by progressive thinkers. For example, later theorists have advanced Dodd's position arguing that corporate law should control LIO's use and abuse of supply chains in contemporary society.²⁴² For the most part, progressive thinkers have not sought to destroy the corporate form, or to eject shareholders from the corporation; rather, their objective has been to find ways to include other parties whose rights and interests

²³⁵ BERLE & MEANS, *supra* note 4, at 6.

²³⁶ C.A. Harwell Wells, *The Cycles of Corporate Social Responsibility: An Historical Retrospective for the Twenty-first Century*, 51 U. KAN. L. REV. 77, 80 (2002).

²³⁷ See Dodd, *supra* note 4.

²³⁸ Wells, *supra* note 236, at 87 (discussing Dodd).

²³⁹ The concern about LIO exerting regulatory authority on society and other actors is part of the issue with their efforts to regulate supply chains. See, e.g., Anne Tallontire, *CSR and Regulation: Towards a Framework for Understanding Private Standards Initiatives in the Agri-Food Chain*, 28 THIRD WORLD QUARTERLY (2007). See also Michael P. Vandenbergh, *The New Wal-Mart Effect: The Role Of Private Contracting In Global Governance*, 54 UCLA L. REV. 913 (2007).

²⁴⁰ Chen & Hanson, *supra* note 6, at 35.

²⁴¹ Wells, *supra* note 236.

²⁴² See sources cited, *supra* note 239.

are affected by LIO. Further, it is important to note that the focus of progressive corporate law scholarship has been on the large corporate enterprise.²⁴³

In essence, the contest could be considered as a contest about corporate models answering the questions: What is the corporation? What are its purposes? Whose concerns should be included? And, how should those persons be taken into account? In other words, the issue becomes one of the politics of corporate law,²⁴⁴ and in particular, the public-ness of LIOs and hence, the corporations that house them. It asks: how public are the powers and functions being exercised by management? What are appropriate corresponding public accountabilities? And, what is a better way to determine this corporation's role in society.

Thus, in terms of CSR, the insider-outsider distinction is considered through stakeholder theory and concerns about political representation.²⁴⁵ Stakeholder theory posits representation in corporate decision-making on a number of different grounds.²⁴⁶ These include the inclusion of those affected by the decision, and those with investments of various types (e.g. labour, finance and community in the corporation and grants power to influence decisions.)²⁴⁷

Unlike like corporate law, however, CSR offers no decision-making structures or processes.²⁴⁸ Rather, it offers an area of contest between corporate advocates and others who have a broader conception of the role of business in society. To this latter group, access to decision-making via a reform of structures and processes is viewed as a highly desirable solution to the problems of LIO, forcing it to control its externalities. Stakeholder theory allows a normative re-ordering which would not necessarily give preference to economic gains above all others. Of course, LIOs have no interest in allowing access to decision-making processes where there is any threat to the normative economic agenda.²⁴⁹

Where there is political agreement that the sole or overriding purpose of the LIO is wealth maximisation, and not the efficient production of necessary goods or services, the regulatory decision-making processes and structures will do little more than allow input as to the best means to achieve that end. Where there is contest about the norms to be taken into account, (for example, where consideration of such things as the environment, labour interests, etc. are introduced) the politics of regulation can and will be of significance. With no

²⁴³ Wells, *supra* note 236, at 78-80.

²⁴⁴ JOHN E. PARKINSON et al., *THE POLITICAL ECONOMY OF THE COMPANY* (Hart Publishing 2000).

²⁴⁵ Benedict Sheehy, *Scrooge – The Reluctant Stakeholder: Theoretical Problems in The Shareholder-Stakeholder Debate*, 14 U. MIAMI BUS. L. REV. 193, 200 (2005).

²⁴⁶ R. EDWARD FREEMAN, *STRATEGIC MANAGEMENT: A STAKEHOLDER APPROACH* (Pitman 1984).

²⁴⁷ Sheehy, *supra* note 245.

²⁴⁸ Teubner suggested a way of moving beyond the CSR stalemate about organisational construction or arrangements and the object or focus of directors duties by shifting the discussion laterally. He suggested that duties be changed substantively to process model. Teubner, *supra* note 77, at 166.

²⁴⁹ Soule argues that there may be a broader social agenda at work. SOULE, *supra* note 5, at 155-4.

clear conception of the entity to be regulated and no agreement on either decision makers or the normative basis for their decision-making authority, it is unsurprising that CSR has less to offer substantively in terms of the main issue, externalities. These issues sit at the foundation of the political criticisms of private regulation. Who is to determine what externalities will be dealt with, by whom and at what price? As one scholar put it, “CSR we contend encompasses contradictory moments with tendencies toward greater democratic accountability as well as toward privatized unaccountable power.”²⁵⁰ How then are we to move forward?

Characterising this issue from a regulatory perspective, it is clear that there is no normative policy consensus. As such, it is impossible for CSR scholars to articulate a unified position on regulation of LIO via internal decision-making. A public alternative has not yet been developed: CSR has no central authority or coordinating body.²⁵¹ Efforts such as the UN’s Global Compact on the public side, or ISO 26000 on the private side, lack power and legitimacy to re-organise internal decision-making processes. Further, a cornerstone of much thinking has been that CSR must be “voluntary” with a range of explanations and justifications given.²⁵² In that diverse context, CSR is best described as a polycentric, loosely networked regulatory initiative. CSR’s difficulty in dealing with these issues is a serious weakness not only in its regulatory power but also in its theory.

c. Construal of Industrial Organisation: Corporate Models

As noted, law and CSR have markedly different conceptions of the problem. While law does not see a problem with the actor, but instead sees problems distributed throughout society, CSR focuses on the actor— LIO. Law, as noted, views the corporation as a legal individual like any other legal individual subject to no specific discriminatory constraints nor receiving any undue privileges. The corporation is long ago settled and decided. Unlike law, CSR does not have clear sense of either the LIO or the corporation.²⁵³ CSR prefers to discuss the corporation as somehow equated with the LIO. To understand this conception, it is helpful to turn to Windsor who identifies political, ethical and economic models of the corporation.²⁵⁴ These models are far from a congruent set and do not match the corporation of corporate law. We discuss each in turn.

²⁵⁰ D. Levy & R. Kaplan, *Corporate Social Responsibility and Theories of Global Governance: Strategic Contestation in Global Issue Arenas*, in OXFORD HANDBOOK OF CORPORATE SOCIAL RESPONSIBILITY 442 (Andrew Crane et al. eds., 2008).

²⁵¹ A problem noted by Prakash Sethi, among others. See Sethi, *supra* note 9.

²⁵² Sheehy, *supra* note 125, at 640.

²⁵³ *Id.*

²⁵⁴ See D. Windsor, *Corporate Social Responsibility: Three Key Approaches*, 43 J. MGMT. STUD. 93 (2006).

The political model is a LIO using a corporation, which is so organised as to include all members of society affected by that industry's activity.²⁵⁵ Given the ubiquity of the corporate form, its outputs, and effects in all things from policy to income distribution, this model has justification. Taking this view potentially shifts the whole of corporate production and distribution from the private sector back into the public sector—a model rejected in capitalist economic subsystems but not by democratic theory.²⁵⁶ While in fact democracy is probably better served by making those decisions explicitly political and deciding as a polity on that basis,²⁵⁷ such an outcome is most unlikely to eventuate.²⁵⁸

The ethical model adopts a human or ecological model of LIO and its membership. All ecologies or human parties impacted by the organisations' ecological footprint need to be taken into consideration in decision-making.²⁵⁹ This model forms a foundation for discussion of sustainability; however, it serves no better than the previous model as identifying the object of regulatory attention. It provides no boundaries and leaves the regulator in the default position of being responsible for the “regulation of everything.”²⁶⁰

The economic model of the firm, which economists purport to be the equivalent of the legal corporation,²⁶¹ also has a different view of the corporation and LIO. Rather than a specific organisation within a market economy, the economic view is that the firm is nothing more than a nexus of contracts.²⁶² That is, in the economic space - although it is a rather densely contracted space - it remains nothing more than individuals contracting together. From this perspective, law's “insider-outsider” distinction makes little sense. Either one has contracted for benefits and liabilities, or one has not. The corporation is only contracts and its regulation is simply a matter of making, performing, and - where necessary - enforcing those contracts. In this model, failure to enter contracts for a clean environment or safe working conditions are failures to create, distribute, and provide contracting mechanisms for the buying and selling of property and *in personam* rights. So, in contrast to corporate law, which creates a separate legal entity and marks its boundaries, CSR offers a trilogy of competing models of industrial organisations.

²⁵⁵ This model can be loosely equated with the stakeholder model. See Sheehy, *supra* note 245.

²⁵⁶ RULING AMERICA: A HISTORY OF WEALTH AND POWER IN A DEMOCRACY (Gary Gerstle & Steve Fraser eds., Harvard University Press 2005); PHILLIPS, WEALTH AND DEMOCRACY: A POLITICAL HISTORY OF THE AMERICAN RICH (Broadway Books 2003).

²⁵⁷ DAVID SCHWEICKART, AFTER CAPITALISM (Rowman and Littlefield 2d ed., 2002).

²⁵⁸ At least at first, Gerstle & Fraser, *supra* note 256.

²⁵⁹ See Windsor, *supra* note 254.

²⁶⁰ LAKOFF, THE ALL NEW DON'T THINK OF AN ELEPHANT!: KNOW YOUR VALUES AND FRAME THE DEBATE (Chelsea Green Publishing 2014).

²⁶¹ Joo, *supra* note 85.

²⁶² Eugene F. Fama, *Agency Problems and the Theory of the Firm*, 88 J. POL. ECON. 288 (1980).

This lack of conceptual clarity concerning the focus of CSR organisational concern undermines its ability to exert regulatory power.²⁶³ Should it focus on directors, the legal person, an association of such persons (i.e. LIO), products, policies, industry, or some other actor?²⁶⁴ Further, the issue of boundaries is an important one about insiders or outsiders. The concern about insiders and outsiders is a concern about power in decision-making and in particular, norms that underlie decisions. The regulatory issues of who, what and on what basis are to be included in decision-making is normative and cannot be settled on terms internal to the debate. It is purely political and as such only susceptible to that type of resolution. This point leads to the discussion of decision-making.

X. SYSTEMS' REGULATORY SOLUTION

The paper thus far has discussed the nature and structure of society's systems, and the role of LIO as the economic subsystem's primary actor. The issue has been characterised as the economic subsystem encroaching upon the political, social, legal and ecological systems, and in doing so, encroaching on the neighbouring political subsystem forcing the retreat of the state and thereby undermining the social system. It subverts a society's culture to achieve business ends of mass culture,²⁶⁵ conceptualises humans as consumers rather than political, biological and social beings, and co-opts the legal subsystem by introducing efficiency as the fundamental norm.²⁶⁶ It is clear that systems—from ecological,²⁶⁷ to economic²⁶⁸, to political—cannot sustain themselves in the current configuration, and require something more.

That something more, contrary to Luhmann's idea of auto-poetic, self-regulating systems, is some type of consciously designed regulatory solution.²⁶⁹

This regulatory role is something Polanyi saw as critical to protecting society from an overreaching market economy. He explained the relationship between land, society and market as follows:

“what we call land is an element of nature inextricably interwoven with man's institutions. To isolate it and form a market for it was

²⁶³ Argument made in Sheehy, *supra* note 125.

²⁶⁴ SOULE, *supra* note 5, at 54.

²⁶⁵ As argued in the informative text on PR STUART EWEN, PR! A SOCIAL HISTORY OF SPIN (Basic Books 1996). The argument has also been made in the legal context, see for example, GUNTHER TEUBNER, GLOBAL LAW WITHOUT A STATE (Dartmouth Publishing Group 1997).

²⁶⁶ As is the foundation of the Law and Economics movement. See for example, POSNER, *supra* note 105.

²⁶⁷ OSTROM, *supra* note 91.

²⁶⁸ See Granovetter, *supra* note 70.

²⁶⁹ For a contrary view, see Newell, *supra* note 229.

perhaps the weirdest of all . . . undertakings. . . life and nature form an articulate whole. Land is thus tied up with the organizations of kinship, neighbourhood, craft, creed—with tribe and temple, village, guild, and church. One Big Market. . . is an arrangement of . . . factors [which] happen to be indistinguishable from the elements of human institutions, . . . and nature.”²⁷⁰

He continues: “the economic function is but one of many vital functions of land. It [land] invests man’s life with stability; it is the site of his habitations; it is a condition of his physical safety; it is the landscape and the seasons.” Polanyi described society’s “double movement” where law, among other institutions, was capable of performing both protective as well as exploitative functions.²⁷¹ As he saw it: “the purpose of the intervention was to rehabilitate the lives of men and their environment, to give them some security. . . [and] introducing public control of national resources”.²⁷² While referring specifically to inter-war Germany, this function of regulation, he argues, is consistent.

Thus, what is lacking is a systems approach to a solution. A systems framework, applicable to Social-Economic Subsystems (SES), has been developed by Elinor Ostrom. For such systems, she has identified eight “design principles.”²⁷³ These are:

1. Clearly defined boundaries (effective exclusion of external un-entitled parties);
 2. Rules regarding the appropriation and provision of common resources that are adapted to local conditions;
 3. Collective-choice arrangements that allow most resource appropriators to participate in the decision-making process;
 4. Effective monitoring by monitors who are part of or accountable to the appropriators;
 5. A scale of graduated sanctions for resource appropriators who violate community rules;
 6. Mechanisms of conflict resolution that are cheap and of easy access;
- Self-determination of the community recognized by higher-level authorities;

²⁷⁰ POLANYI, *supra* note 41, at 187.

²⁷¹ *Id.* at 233.

²⁷² *Id.* at 225.

²⁷³ These were designed to solve for problems in the limited context of common pool resource management. OSTROM, *supra* note 91.

7. In the case of larger common-pool resources, organization in the form of multiple layers of nested enterprises, with small local CPRs at the base level.²⁷⁴

While Ostrom's framework is designed for specific common pool resources, it may also be broadly applied to the ecology as a whole. The foregoing analysis is not to jettison Luhmann's work. Indeed, a solution can be achieved by bringing Luhmann and Ostrom together, to identify the problem clearly. It may be characterised using Luhmann as a problem resulting from the failure of the economic subsystem's self-regulation and an excessive disappointment of expectations in law. Drawing from Ostrom's perspective, it is a failure to adequately protect the common resource of the ecology from exploitation for purposes of economic profits, described in economic terms as a collective action problem—a systems integration problem. Polanyi contributes to this discussion by providing the historical political background—he explains how the economic subsystem came to be disembedded from the social and natural environments.²⁷⁵ The issues so framed can be addressed by an institutional view of regulation.²⁷⁶ What Ostrom's institutional efforts²⁷⁷ focus on is precisely what Teubner saw as the problem addressed by CSR—re-embedding the economic subsystem.²⁷⁸

This re-embedding will require ecological jurisprudence,²⁷⁹ ecological economics²⁸⁰ and political theory,²⁸¹ which in turn will have to lead to law

²⁷⁴ OSTROM, *supra* note 91.

²⁷⁵ POLANYI, *supra* note 41.

²⁷⁶ Schneiberg & Bartley, *supra* note 147.

²⁷⁷ Amy R. Poteete & Elinor Ostrom, *Heterogeneity, Group Size and Collective Action: The Role of Institutions in Forest Management*, 35 DEV. & CHANGE 435 (2004).

²⁷⁸ Daniel P. Kinderman, *Re-Embedding of Dis-Embedding the Corporation? The Transnational Social Networks of Corporate Responsibility Across Europe: 1982-2007*, APSA 2010 ANNUAL MEETING PAPER, <http://ssrn.com/abstract=1643059> (last updated Feb. 20, 2013); Amstutz, *supra* note 110. Dirk Matten & Jeremy Moon, *A Conceptual Framework for Understanding CSR*, in CORPORATE SOCIAL RESPONSIBILITY ACROSS EUROPE (A Habisch et al. eds., 2004); Rawl Abdelal & John G. Ruggie, *The Principles of Embedded Liberalism: Social Legitimacy and Global Capitalism*, in NEW PERSPECTIVES ON REGULATION (David Moss & John Cisternino eds., 2009). Such re-embedding, it is argued, would reduce corporate scandal and collapse. Michael Gonin et al., *Neither Bad Apple Nor Bad Barrel: How the Societal Context Impacts Unethical Behavior in Organizations*, 21 BUS. ETHICS: A EUR. REV. 31 (2012).

²⁷⁹ Samuel Alexander, *Earth Jurisprudence And The Ecological Case For Degrowth*, 6 J. JURIS. 31 (2010); CORMAC CULLINAN, *WILD LAW: A MANIFESTO FOR EARTH JUSTICE* (Siberink 2002); CHRISTOPHER STONE, *SHOULD TREES HAVE STANDING? AND OTHER ESSAYS ON LAW, MORALS, AND THE ENVIRONMENT* (1996).

²⁸⁰ Miriam Kennet & Volker Heinemann, *Green Economics: Setting the Scene. Aims, Context, and Philosophical Underpinning of the Distinctive New Solutions Offered by Green Economics*, 1 INT. J. GREEN ECON. 68 (2006).

reform. In terms of corporate law, Greenfield has argued that reform needs a different footing.²⁸² How can these systems be reconnected? At the core of the problem has been a failure of regulation in terms of regulating the systems, which support human life on the planet. Accordingly, the core of any solution must be built around the creation of a regulatory system with its three parts: first, **processes** of norm generation, a consensus on objectives and then a decision about techniques.²⁸³ These are followed by an evaluation process built-in so that those generating the norms can inquire whether the techniques have been successful in achieving the objectives. Second, **components** to organise management of the processes just identified with institutional infrastructure. And finally, a regulatory system needs to be appropriately **energised** to motivate the desired behaviour.

Answers with respect to all aspects of this new regulatory system are forthcoming from all quarters, although challenged by elite interests.²⁸⁴ In terms of the **processes**, these are well underway. Thinkers such as Stiglitz see the need to integrate social needs and environmental challenges of global warming into globalisation.²⁸⁵ Green economics, for example, is described in exactly these terms: “Green Economics seeks to reconnect the values and costs of transactions with the natural world and with social structures. It seeks to enhance the local economy; supports bio-regional developments, democracy and access for all; and seeks global governance through new institutions designed for this purpose.”²⁸⁶

Ecological jurisprudence is a jurisprudence not based on ideology of liberal philosophy; rather, “ecological jurisprudence aims to bring considerations of justice to the foreground . . . ultimately grounded in empirical analysis rather than mere ideology.”²⁸⁷ In other words, conditions of the ecology more widely may be considered by the courts.²⁸⁸ Production could occur within more

²⁸¹ ALPEROVITZ, *AMERICA BEYOND CAPITALISM: RECLAIMING OUR WEALTH, OUR LIBERTY, AND OUR DEMOCRACY* (2005).

²⁸² GREENFIELD, *supra* note 16.

²⁸³ *A Normative Theory*, *supra* note 18.

²⁸⁴ ALPEROVITZ, *supra* note 281.

²⁸⁵ JOSEPH E. STIGLITZ, *MAKING GLOBALIZATION WORK* (Penguin Books 2006).

²⁸⁶ Kennet & Heinemann, *supra* note 280.

²⁸⁷ Although focused on domestic violence, the article’s principles are widely applicable. Mark Fondacaro, *Toward an Ecological Jurisprudence Rooted in Concepts of Justice and Empirical Research*, 69 UMKC L. REV. 179 (2000-2001).

²⁸⁸ The limitations on judicial consideration of non-law sources was limited by the doctrine of “judicial notice” perhaps first extended by the Brandeis Brief. In Canadian corporate law, two significant Supreme Court of Canada decisions have extended the consideration of directors’ decision-making discretions. See *BCE Inc. v 1976 Debenture Holders* (2008) 3 S.C.R. 560 (Can.). Indeed, there are sound legal reasons for directors to take account of such issues. Benedict Sheehy & Donald P Feaver, *Anglo-American Directors’ Legal Duties and CSR: Prohibited, Permitted or Prescribed?*, 37 DALHOUSIE L. J. 1 (2014).

democratically organised enterprises as cooperative structures would suggest,²⁸⁹ and perhaps be extended beyond even those directly involved in production. Essentially, what would then occur would be a clearly defined boundary for economic activity. That boundary would be defined both in social and ecological terms, and not simply economic.²⁹⁰ Interestingly, law has already done so to some extent. Law and economics scholars note inalienable rights—rights that should not be commoditised.²⁹¹ Extending the ambit of inalienable rights beyond certain individual rights, critically, would require a re-ordering of normative priorities. The priorities could not be set as a private matter to avoid the democratic deficit of CSR.²⁹² Rather, the normative ordering process would need to be inclusive. Following principles of sustainability, preservation of the ecology would be the first principle. It would be considered a public right, and would so be prioritised ahead of private rights and ahead of economics.

Drawing further from the discussion of the LIO and of the corporation, in terms of objectives, consensus may be reached, perhaps following Brandeis' earlier suggestion that organisations not be permitted to become too large. In essence, a business that is “too big to fail” is too big to be private: one of the important lessons from the latest financial crisis is that public funds will be expended to rescue private LIOs, which are too big to fail. Too big is also a political determination—too big to fail might be “too big” in terms of political power. The old saying, “power corrupts and absolute power corrupts absolutely”, suggests not only that individuals cannot be trusted with too much power, but that organisations too need to be restrained from excessive size, and hence garnering excessive power. Finally, “too big” may refer to ecological footprint.²⁹³ LIO with excessive ecological footprints could be determined excessively detrimental to the ecology and so terminated as either a particular business or even an industry.²⁹⁴ Both of the insights concerning inalienability and limiting the size of organisations could be legislated realising Luhmann's “immunisation” function

²⁸⁹ WILLIAM WHYTE & KATHLEEN WHYTE, *MAKING MONDRAGON: THE GROWTH AND DYNAMICS OF THE WORKER COOPERATIVE COMPLEX* (ILR Press 1991). But note too the necessity for contextualisation of cooperatives. SHARRYN KASMIR, *THE MYTH OF MONDRAGON: COOPERATIVES, POLITICS, AND WORKING-CLASS LIFE IN A BASQUE TOWN* (State University of New York Press 1996).

²⁹⁰ HERMAN DALY & JOHN COBB JR., *FOR THE COMMON GOOD: REDIRECTING THE ECONOMY TOWARD COMMUNITY, THE ENVIRONMENT, AND A SUSTAINABLE FUTURE* (Beacon Press 1989).

²⁹¹ Guido Calabresi & A. Douglas Melamed, *Property Rules, Liability Rules and Inalienability: One View of the Cathedral*, 85 HARV. L. REV. 1089 (1972). See also Susan Rose-Ackerman, *Inalienability and The Theory of Property Rights*, 85 COLUM. L. REV. 931 (1985).

²⁹² Palazzo & Scherer, *supra* note 162.

²⁹³ PAUL HAWKEN, *THE ECOLOGY OF COMMERCE: A DECLARATION OF SUSTAINABILITY* (HarperCollins 1993).

²⁹⁴ RAY C. ANDERSON, *CONFESSIONS OF A RADICAL INDUSTRIALIST: PROFITS, PEOPLE, PURPOSE: DOING BUSINESS BY RESPECTING THE EARTH* (St. Martin's Press 2009).

of law.²⁹⁵ That is, by embedding these as legal norms, such a reform could immunise society against their recurrence in the future.

As to the second aspect of regulatory systems, the **components**, we may again draw from CSR ideas. The regulatory infrastructure would be less embedded in the political system and more embedded in community. It would include more coordinating mechanisms and organisations to help all actors collaborate—high-level political actors from the UN down to local community members, to producers of all sorts. Rule-making would be done collaboratively by those close to the location of operations, with input from, and support of, experts and higher authorities so that appropriate adaptation to local conditions could be made.²⁹⁶ Substantive rights in the environment could be more broadly distributed.²⁹⁷

In terms of procedure governing decision-making processes, a broader collective would be involved which may decide to make “prevention” primary—an executive action. This approach would largely displace the current adjudicative legal processes involving post facto ad hoc compensation. Further in terms of executive functions, it would require monitoring of some sort, possibly in line with a public interest group espoused by Ayres and Braithwaite as a new regulatory method.²⁹⁸ This new structure and process could draw from the CSR discussions on participation in decision-making.²⁹⁹ It would require modification of existing corporate law doctrines if the new production were to be housed in the legal corporation.³⁰⁰

In line with the new thinking about regulation, there is a considerable role to be played by innovative development of institutions. What would be an appropriate institutional form, however, is not clear. Although institutions like the UN have initiated programs like the Global Compact³⁰¹, the Global Reporting

²⁹⁵ Luhmann looks at the immunisation function as an internal protective function but sees law as having this potential to immunise the social system. LAW AS A SOCIAL SYSTEM, *supra* note 66, at 475.

²⁹⁶ See, e.g., Gulbrandsen, *supra* note 200.

²⁹⁷ Such rights need not be limited to property rights as advocated by economists following Garrett Hardin, *Tragedy of the Commons*, 162 SCIENCE MAG. 1243 (1968). A basic criticism of Hardin and other property rights advocates is that what motivates spoiling of the commons in the first instance is the introduction of the profit motive. Without such, people tend to care for collective resources.

²⁹⁸ IAN AYRES & JOHN BRAITHWAITE, *RESPONSIVE REGULATION: TRANSCENDING THE DEREGULATION DEBATE* (Oxford University Press 1992).

²⁹⁹ See Sheehy, *supra* note 245.

³⁰⁰ Andreas Georg Scherer & Guido Palazzo, *The New Political Role of Business in a Globalized World: A Review of a New Perspective on CSR and its Implications for the Firm, Governance, and Democracy*, 48 J. MGMT. STUD. 889 (2011).

³⁰¹ United Nations Global Compact, <http://www.unglobalcompact.org/> (last visited Jan. 27, 2017).

Initiative,³⁰² and International Standards Organisation its ISO 26000,³⁰³ the success of these programs is somewhat limited.³⁰⁴ These initiatives represent an important first step—institutionalising a practice of reporting on social and environmental impacts. Such a disclosure regime could follow a trajectory similar to the development of corporate financial reporting, which was used to clean up financial wrongdoing after the Wall St crash of 1929.³⁰⁵ These reporting initiatives could be strengthened if they were to engage in national law, the home of the legal corporations as well as nation-states where LIOs operate. Institutions may be more effective where national bodies are engaged,³⁰⁶ or if more innovative regulatory thinking were to be applied.³⁰⁷

In terms of **motivations**, bringing together the analysis of the two regulatory systems, certainly additional options are opened up. Both public and private resources could be combined not only to constrain the producer organisations, but also to facilitate their contribution to the community more broadly.³⁰⁸ Such contributions could include certain types of services: from day care to hosting visitors, distributing employment more equitably, to supporting educational and other forms of community development. Public law could be modified to prefer such types of organisations through tax laws, and other benefits, which could more effectively support such organisations. Public law could further be designed to facilitate both prior prevention as well as broader

³⁰² Carol Adams & Liliana Petrella, *Collaboration, Connections and Change: The UN Global Compact, the Global Reporting Initiative, Principles for Responsible Management Education and the Globally Responsible Leadership Initiative*, 1 SUSTAINABILITY ACCT. MGMT. & POL'Y J. (2010); Halina Szejnwald Brown et al., *The Rise of the Global Reporting Initiative: A Case of Institutional Entrepreneurship*, 18 ENVTL. POL. 182 (2009).

³⁰³ The process by which the ISO 26000 was developed was a concern among participants. See Halina Ward, *The ISO 26000 International Guidance Standard on Social Responsibility: Implications for Public Policy and Transnational Democracy*, 12 THEORETICAL INQUIREIS INTO L. 665 (2011).

³⁰⁴ Ralf Barkemeyer, *Beyond Compliance – Below Expectations? Cross-Border CSR, Development And The UN Global Compact*, 18 BUS. ETHICS 273 (2007). It was anticipated that ISO 26000 would fail to achieve substantial outcomes. Pavel Castka & Michaela A. Balzarova, *The Impact of ISO 9000 and ISO 14000 on Standardisation of Social Responsibility—An Inside Perspective*, 113 INT'L J. PRODUCTION ECON. 74 (2008).

³⁰⁵ Henry Laurence, *Spawning the SEC*, 6 IN J. GLOB. LEGAL STUD. 647, 656 (1999).

³⁰⁶ There is growing public law interest in regulating CSR. See, e.g., Corporate Social Responsibility Disclosure Efforts By National Governments And Stock Exchanges, INITIATIVE FOR RESPONSIBLE INV. (2015), http://iri.hks.harvard.edu/files/iri/files/corporate_social_responsibility_disclosure_3-27-15.pdf. Canada nearly went in this direction with Bill C-300: Sound and Measures Reinforcement for CSR: A Report on the Legal and Policy Dimensions of Bill C-300 (Sept. 2009).

³⁰⁷ *A Normative Theory*, *supra* note 18.

³⁰⁸ In this context, several works show ways forward and promise Burger et al., *supra* note 200; JOHN J. KIRKTON & MICHAEL J. TREBILCOCK, *HARD CHOICES, SOFT LAW: VOLUNTARY STANDARDS IN GLOBAL TRADE, ENVT. & SOCIAL GOVERNANCE* (Ashgate 2004).

participation in litigation where the ecology is harmed. In other words, both substantive and procedural law could be reformed to achieve such ends. These reforms would help implement Ostrom's principle of dispute resolution being cheap and accessible—a fundamental principle of law. While none of these ideas is new alone, and for the most part appear to be a long way from the present order, the paper provides a new way of understanding the problem and organising a solution. Given the history of change, there is reason for optimism.³⁰⁹

XI. CONCLUSION

The problem, in a nutshell, is that the economic subsystem has undermined the viability of the political, social, legal and ecological systems through conceiving itself as tasked with wealth creation. In so conceiving itself, it has forced the retreat of the state, manipulated culture, and re-shaped thinking about humanity. Part of what has become evident is that negative externalities of LIOs are often seen as a matter of corporate activity. The solution from this perspective is the revision and reform of corporate law.

The regulation of LIO, however, is clearly a highly complex matter. Public efforts at regulation through the legal subsystem clearly leave much to be desired. The failure of the legal subsystem to adequately address the LIO's externalities and its facilitation of those externalities by its creation and characterisation of the corporation as a private law matter have led to the social outcry calling for more, or perhaps different, control of the corporate form.

By the same token, CSR as private regulation is problematic. CSR is problematic not only because it lacks any coherent norm generating and sorting processes, or institutional infrastructure, but also because it is unclear about fundamental issues such as wealth creation, appropriate control over production and distribution of goods and services, or the priority to be given to the ecology necessary for human life across the generations.

Taking the foregoing analysis and putting it into a systems perspective gives unique insight into the problem and the peculiar role of the legal corporation. The economic and legal subsystems share a boundary along the border of corporate law. Being so located at the boundary of the public legal and private economic subsystems allows this lego-economic actor particular powers to interact with the social system as a whole and facilitates the economic subsystem's encroachment on neighbouring systems.

From a systems perspective CSR is a response to law's failure or inadequacy in terms of regulating LIO. It fills the gaps and takes a different ex ante preventative approach. It is what Polanyi describes as a "double movement", or perhaps a Hegelian antithesis or reaction, to the massive social and

³⁰⁹ At least at first, GERSTLE & FRASER, *supra* note 256.

environmental footprint of LIO. The issue diagnosed as such is both a systems issue as well as a matter of public institutions. Such issues call for systemic and public institutional solutions, a public regulatory response. Given the power imbalance and the highly variable environment in which such a regulatory response would occur—i.e. the specific industry and specific LIOs with their particular social and environmental footprints, problems and contributions, a broad public law solution is unlikely to achieve the rebalancing. It is unlikely that it can be (or should be) done without input from both LIO *and other interested local parties*—too often non-industry participants are left out of the discussion. In summary, some governmentally coordinated regulatory response is called for. The nature and design of such regulation, however, is a matter for another paper.

The task at hand, dealing with the three issues of social costs, concentrations and the role of law (including the corporation), can be cast as the issue of the regulation of the LIO housed in a legal corporation. The LIO organised in the corporate form can be described as a product of the one subsystem, the legal subsystem, and the dominant participant of the other, economic subsystem. As such it is subject to two subsystems each with its own norms—a private person in the one, and pursuing profits without restraint in the other. These two normative priorities and perspectives make it particularly difficult to regulate the corporate LIO effectively. The regulatory systems compete to impose their lenses as exclusive means for regulating the LIO housed in the legal corporation.

Further, each of these public and private regulatory efforts has its own agenda driven by the norms of the subsystem it serves. Law on the one hand pursues regulation in a way that is coherent with the legal subsystem and is consistent, attending to both the doctrines and principles, including its liberal political philosophy, which it has developed over the centuries. It operates largely as Luhmann would suggest —i.e. as a self-referential system, and as a complaint driven process through which liberal individuals pursue their specific grievances on an ad hoc basis.

The economic subsystem, on the other hand, as a burgeoning and colonising subsystem has shifted from a focus on production to wealth creation. The economic subsystem has co-opted both legal and political subsystems to serve itself. It has failed to operate as Luhmann's self-regulating subsystem, attending to performance, function and it has failed to demonstrate the third feature of systems—the self-reflective or self-referential. In the case at hand, the changes to the social system identified as the first and second issues addressed by

CSR—social costs and wealth inequalities—have led to an inability for the social system to operate as it should, to sustain human life in the long run.³¹⁰

Any reform seeking to address these issues will rely critically on a re-norming and consequent reconceptualising of the economic subsystem. The economic subsystem's function needs to be shifted from wealth generation based on unlimited growth to provisioning human needs, including the needs of subsequent generations, and working within the limited ecological capacity of the planet. In terms of the economic subsystem's performance, such performance can no longer be measured against the previous year's growth, a performance that can only be achieved by more commoditising goods and services in neighbouring subsystems. Rather, performance must be measured against the economic subsystem's ability to sustain other social systems. Steps in this direction, however halting and mistaken, such as the Index of Sustainable Economic Welfare³¹¹ among others³¹² have already been taken.

To achieve any such reform is ultimately and intimately an institutional matter.³¹³ Institutions such as both the legal corporation and the LIO are contested. Further, the institutional systemic public law and private initiatives such as CSR have a great role to play. Reaching a consensus on any reform agenda is difficult. Even consensus on what would seem incontrovertible to some, the fundamental principle that human life looked at in the longer term must be the starting point for all regulation, public or private, is not simple. Yet as distant as these things may seem, at least as touching the LIO, the first step of developing a consensus does not appear as far removed from the normative core of CSR as it once was.

³¹⁰ WALTER F. BABER & ROBERT V. BARTLETT, *GLOBAL DEMOCRACY AND SUSTAINABLE JURISPRUDENCE: DELIBERATIVE ENVIRONMENTAL LAW* (Massachusetts Institute of Technology 2009).

³¹¹ DALY & COBB JR., *supra* note 290.

³¹² See discussion in PORRITT, *CAPITALISM: AS IF THE WORLD MATTERS* (2005).

³¹³ Schneiberg & Bartley, *supra* note 147.