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The State as ‘Black Box’ and the Market as Regulator:
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Abstract: In the autumn of 2008, at a time of global reconsideration of the role of states in the regulation of markets, the paper uses the reflection on past experiences with the laissez faire state, the interventionist state, the welfare state and the enabling state as institutional crystallization points in an ongoing learning process of regulatory innovation as a framework to assess contemporary proposals to delegate public international law [PIL] enforcement to market actors. As such, the paper attempts to carve out possible conceptual and political implications of the current proposals against the background of interventionist and post-interventionist market regulation models. However, the translation of nation-state experiences with market regulation onto the global sphere presents a challenge in light of the particular structural qualities of transnational regulatory regimes. The task – both for a reconstructive narrative and for a delegation theory of PIL regulation through market actors – lies in the production of a better understanding of state-market and public-private distinctions in the transnational arena.

Keywords: Public International Law Enforcement, Market regulation, Interventionist State, Transnational Law, Regulatory Theory, Governance

JEL classification: K33, F55, F59

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I. MARKETS AS REGULATORS

In face of the dramatically challenged and tired body of the international legal order (GOLDSMITH AND POSNER [2005]), searches for its reinvigoration, healing or overhaul are well under way. While the assessment of itsailings has been occupying public international law [PIL] and international relations scholars for a long time (HUDSON [1925], GOLDSTEIN et al. [2000], KOSKENIEMI [2002], VAN AAKEN [2006], MILLER AND BRATSPIES [2008]), the intervention of law & economics scholars onto the scene is of more recent venue (SCOTT AND STEPHAN [2006], GUZMAN [2008]). Professor van Aaken’s suggestion to explore the potential of market mechanisms to effectuate international legal regulation occurs against the background of this more recent conceptual intervention. The following observations will attempt to discuss her proposal by revisiting some of PIL’s and international relations’ longer standing concerns about an effective legal order.

II. LAW’S DREAM AND MARKET REALITIES

VAN AAKEN [2009] draws our attention to a number of market-driven mechanisms that might be able to give PIL substantive impulses and new life. Her examples include the private industry complaint processes around the WTO’s Dispute Settlement Body, the Financial Action Task Force and the Kimberly Process Certification Scheme. Her interest in these examples is the result of changing the analytical lenses through which we have been trying to make sense of the double-movement that characterizes the transformation of the international legal order. On the one hand, we are

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faced with the urgent need to make the regime responsive and receptive to emerging (and persisting) claims for recognition, rights and identity, some of which might pose insurmountable challenges to PIL’s declared universalist and cosmopolitan aspirations (HELD [1995, p. 141], HABERMAS [2006, p. 5]). On the other hand, the very idea of thinking of a body of international law that would bear resemblances with a contained, historically grown and solidly institutionalized legal order that we tend to recognize within the confines of the Western nation state, fades away under the impression of international law’s eternally volatile and ephemeral character. The fragmentation of (every) law, that – rightly considered – marks the legal project in its foundation, has been pointed to in recent times by international legal scholars in order to critically ascertain the contested nature of the international legal order and to fend off ill-founded rescue attempts in the name of the unity of law (KOSKENNIEMI AND LEINO [2002, p. 553]). The fragmentation of (global) law must in fact be seen as merely another instantiation of the very fragile nature of the legal order as such, regardless of whether our focus is on international or domestic law (ZUMBANSEN [2006a], [2008a]). The doubtless breathtaking proliferation of norm producers, norm entrepreneurs and of alternative processes of norm dissemination and enforcement that we witness on the global level, is only an expression of law’s functional differentiation (TEUBNER [1997a], [1997b]), not an expression of an originally pure and healthy body being impaired.

It is precisely because global law suffers from the same shortcomings and reality shocks that Kafka’s victim is struggling to understand when he finds himself ‘before the law’, that Van Aaken’s intuition to explore alternatives to traditional law enforcement to save the law from its ineffectiveness is correct. That she is willing to entrust the regulation of human affairs in the market, however, bears the risk of substituting one complex regime (“law”, “state”, “rule of law”) with another one (“market”). Her attempt to potentialize ‘market mechanisms’ to strengthen PIL’s application in an unruly world shares some (perhaps unrealized) parallels to prior explorations of the transnational nature of legal relations (JESSUP [1956]). Van Aaken, in scrutinizing market driven mechanisms with view to their potential to create conditions of higher compliance or, at least, of scandalizations of non-compliance, comes close to repeating Philip Jessup’s conceptual move of drawing parallels between conflicts over participation, legitimacy and enforcement within and outside of the nation state in order to expose the fundamental regulatory challenge to all
law. Yet, as Van Aaken relies on a disembedded concept of market mechanisms as enforcement driving, this parallel to the regulatory experiences of the domestic arena remain untapped. And because there is little room in her discussion of PIL’s market-therapy for revisiting the trials and tribulations of state–market relations that have marked Western industrialized welfare states all through the twentieth century, the analysis of the state–market relations in the global arena with changed meanings of sovereignty, contract and the ‘public’ ends too early. The application of a game-theoretical approach to explain the use of self-regulatory governance modes occurs in a highly abstract, purified sphere. In contrast, were we to take Jessup’s cue and consider the deep-running regulatory challenges of the transnational order through a series of connections between governance modes within and outside of the nation state, we would probably be in a better position to evaluate the promises of self-regulation within the international legal order.

III. GOVERNANCE COMING OF AGE

Van Aaken is right to point to the merit and urgency with which we need to take a close look at the emerging, hybrid public–private regulatory regimes that mark the global arena. It is here, where we can hope to find elements of an emerging transnational legal order. Van Aaken’s third example concerning the Kimberly Process Certification Scheme, designed to stem the trade of conflict (“blood”) diamonds, is a perfect illustration of the challenges that we face when reassessing the troubled international legal order. The Kimberly Process, an initiative jointly entertained by governments, industry and civil society, presents us with the dilemma of trying to conceptualize an effective regulatory regime despite the resistance of numerous key-players. As such, her example feeds into and is closely tied to what she refers to as “the whole discussion on Corporate Social Responsibility” (Van Aaken [2009, p. 23]). Yet, what has been both inspiring and plaguing CSR scholars for decades, is the field’s inherent boundarylessness. The most promising approaches to study and belabour CSR, then, are connections such as those drawn by Van Aaken between normative agendas and existing regulatory structures, in particular where those are in constant evolution (Ruggie [2008], Ochoa [2008]). What emerges from this approach is the realization that the potential of CSR to make any meaningful contribution to the ongoing
regulatory transformation (Levy and Kaplan [2008, p. 439]) depends in large part on its capacity to integrate sociological and political economy criteria into its model-building processes. The importance of such an integrated approach to promote CSR is powerfully illustrated by the continued interest in the study of self-regulatory instruments in the context of larger regulatory changes, as exemplified by work on corporate codes of conduct that formulate duties vis-à-vis their employees, the local communities and the environment (Blackett [2004], Arthurs [2002], Zumbansen [2006b]).

This, then, provides the platform on which to comment on the lessons that Van Aaken suggests to draw from such instantiations of market mechanism as drivers of more effective international law regulation: her central claim is that in order to effectuate international sanctions, the system must reach beyond the boundaries of the black box of the “state” and thus “permeate the network of all actors involved, that is, the market forces” (Van Aaken [2009, p. 23]). In order to achieve this result, two conditions must be met: sanctions need to target an end consumer market, and NGOs as independent monitors must ensure a sufficient level of transparency and publicity. In particular, I want to challenge Van Aaken’s suggestion that we need to reach into the state as ‘black box’ in order to understand the potential of market mechanism as regulator.

What is at stake when we speak of the state as a ‘black box’? Van Aaken rightly points to important PIL and IR scholarship that has shown the degree to which contemporary states ‘disaggregate’ (Slaughter [2004]). When speaking of a ‘state’, then, we are dealing with a concept in transformation (Hoffmann [2008, p. 266]). Today, the ‘state’, which in public international law is the sovereign actor, equipped with equal rights, and author of the norms that bind or empower it, looks very different from a functional perspective. From this perspective the state becomes a nodal point for various functional processes, and it is in that regard that the state is constantly being adjectivised (the “social” or, “welfare” state, the “minimal” state, the “enabling” state, the “supervision” state). With regard to the state’s sovereignty, its transformation can be described as a two-way erosion of sovereignty, one upward with regard to a state’s entered into international agreements and accepted or, forced-upon compromises (Summers [2001]), and one downward as concerns the long history of further expanding mixed, public–private, hybrid forms of state–market cooperation and coordination in the delivery of formerly public services and of the state’s myriad forms of intervening into the market (Grimm
[1990, p. 291]). A more recent interpretation points to the increasing
dependence of the state on societal knowledge, the generation of which
becomes one crucial public mandate of the post-welfare state (LADEUR
[2006]), an observation that fares well with the economist’s finding in the
1930s (HAYEK [1937, p. 33], [1945, p. 530]).

IV. FROM GOVERNMENT TO GOVERNANCE – AND
BACK?

Van Aaken differentiates between certain ‘issue areas’, where the
involvement of private actors is allegedly more pertinent than in others.
The assignment of such areas occurs, however, without offering criteria or
categories that can be used to convincingly differentiate between ‘public’
and ‘private’ concerns. In light of our experiences in public and private
law with the ‘mixed economy’ of Western welfare states and the eternal
challenge of these fields’ analytical grip and boundaries, the reliance on
distinctions between issues in the private or the common, public interest
seems to bear little promise. These demarcations have themselves become
very problematic against the background of the changing regulatory
landscape within nation states (GRIMM [1991], LOBEL [2004]). Such
reliance comes back, for example, also in form of the distinctions such as
those that were recently suggested by Gillian Hadfield and Eric Talley
between “economic” and “justice” concerns through which we ought to be
able to assign regulatory competences (HADFIELD AND TALLEY [2006]).

The use of such distinctions is even less warranted in a functionally
highly differentiated Knowledge society. Today’s society cannot on the
one hand, as Van Aaken suggests, be described as a global market society,
if we want to, on the other hand, continue to explain it by reference to
state–market concepts that we have been struggling with all throughout the
history of the social and the welfare state. To confront and to take
seriously, however, the fragmented and functionally differentiated nature
of society is what should follow from the proposal to reach beyond the
state as a ‘black box’. In a transnational regulatory sphere, instead of
recurring to state–society or state–market distinctions, we ought to refocus
on how and under which disguise these former nation state based political
debates might re-appear within the transnational sphere. It is here where
we are in the midst of scrutinizing the role and function of new actors in
PIL, the fuzzy contours of civil society or the changing ways in enhancing
participation and monitoring, for example through a shift to “governance through disclosure” (HERBERG [2007], WERNER [2008]).

To complement the existing, highly contested PIL enforcement mechanisms that play out against the background of the ongoing struggle between hegemony, fragmentation and universalism with private market mechanisms might offer less of a critical basis on which to better understand the challenges of transnational regulation. Instead, we ought to see the PIL system as a ship under repair on high seas, in order to, first, recognize its striking similarities with the legal system currently under scrutiny and attack through private ordering mechanisms which might be developed too much in isolation from and in rejection of the regulatory experiences in the 20th century legal and political orders, in particular the welfare state, and, second, learn to better read the complex forms of emerging forms of transnational governance in highly specialized regulatory fields such as those highlighted in Van Aaken’s paper.

The proposal to reach beyond the state as the central focal point in regulating PIL gains credibility in view of the shift of concepts of government in public international law to those of governance (ENGEL [2001, p. 571], ENGEL AND KELLER (eds.) [2000]). But that shift – from government to governance – creates in fact a number of far-reaching challenges that we must take seriously in our attempt to adequately understand the role of market mechanism in rendering legal regulation more effective. One is that when we speak about the way in which the state as law-maker and law-enforcer in PIL is challenged by and competing with emerging private governance regimes, we have to draw on our experiences with public–private governance, privatization and indirect regulation in our long history of highly complex market regulation. After decades of transforming the interventionist into a moderating, enabling, empowering and bargaining state, there exists plenty of evidence of contractualized and outsourced public functions. Because these have emerged over the last 30 years from within mature constitutional regimes, their direct translatability onto governance issues concerning multinational corporations or transnational trade regimes might be limited. At the same time, it is important to take seriously the persistent conceptual and normative pitfalls that (re-)occur within these transnational regulatory regimes. We would be so naïve to think we can find or perhaps recreate on the transnational plane the same or equivalent institutional, political and legal framework in which struggles over rights, entitlements and redistribution have taken place within the nation-state. Rather, we are
faced with the inevitable recognition that the ways in which we must make choices over how to regulate ‘issue areas’, we are likely to rely concepts and patterns which themselves are deeply embedded in our particular histories of legal, direct and indirect, regulation.

Those histories have of course dramatically different contours with regard to the mix of formal and informal regulation, the institutional environment and the varieties of institutional change (NORTH [2005]). But because we deal on a comparative basis with differences that Hall and Soskice have called, “Varieties of Capitalism” (HALL AND SOSKICE (eds.) [2001]), and which constitute in fact a great range of differently evolved ‘institutional complementarities’ (BOYER [2005, p. 64]), we should not think of the state–market relation in the transnational arena as in any way less complex:

“[M]ost of the institutions that are today perceived as complementary, were in fact created for distinct purposes and only the succession of crises, experiments and sequential innovations finally delivered the complementarity that is recognized at the end of a rather long historical process.” (BOYER [2005, p. 64])

According to Boyer, complementarity, among other factors, provides the glue that holds together a global institutional architecture. Even in an era of globalization, financialization and knowledge-based competitiveness, national economies still exhibit contrasted institutional configurations, and from that it follows that capitalism diversity is not a matter of pure historical legacy, inertia or irrationality.

This means, that the expanded view on PIL enforcement by market mechanisms can learn much from already existing and further emerging private governance regimes in domestic legal orders on the one hand and from comparative political economy on the other. Examples of domestic soft-law and indirect regulation abound, let’s only mention standard setting, food safety, or even corporate governance. Those regulatory fields are increasingly unfolding in a transnational arena. But their apparent borderless nature does not mean that they are not to be associated with a whole range of conceptual and architectural burdens that can only be explained when looking closer at the market–state relationship.
V. THE TRANSNATIONAL TRANSLATION

Among the areas showing great regulatory innovativeness and evolutionary dynamics is corporate governance. Its regulation offers valuable insights into the nature of what should adequately be called “transnational legal pluralism” (ZUMBAUSEN [2008b]). While this term recognizes the multiplicity of normative orders at work in the creation of regulatory regimes, it is also helpful in redirecting our focus to the particular interplay of soft and hard law in these regimes. Corporate governance reveals its complex structure only when we closely follow the genesis of corporate governance norms through the maze of global discussions over convergence or divergence, the scandalization of corporate misconduct and the different national reactions, often resulting in a complex mix of direct and indirect regulation. Corporate governance then unfolds as a prime example of a transnational regulatory regime, can only be understood if we pay close attention to the ways in which the state on the domestic level again and again facilitates and monitors processes of self-regulation. The pressing need to reassert the regulatory structure of such an area stems from the supposedly natural course by which it is said to have been evolving over the past twenty years, that have seen the triumphant march of shareholder value as the exclusive governing principle in corporate law (HANSMANN AND KRAAKMANN [2001]). There is, however, nothing natural about the market and its dynamics. Markets are constituted, property rights are allocated competences and vest public authority in private parties to engage in the distribution of power (HALE [1923, p. 478], COHEN [1927, pp. 11f.]). The breathless emergence of the insatiable market as organizational principle certainly threatened such insights and provided the basis for far-reaching claims as to its superiority in governing human affairs:

“[T]he control of the economic system by the market is of overwhelming consequence to the whole organization of society: it means no less than the running of society as an adjunct to the market. Instead of economy being embedded in social relations, social relations are embedded in the economic system.” (POLANYI [1944, p. 57])

A little later in his text, Polanyi observes:
“With every step that the state took to rid the market of particularist restrictions, of tolls and prohibitions, it imperiled the organized system of production and distribution which was now threatened by unregulated competition and the intrusion of the interloper who ‘scooped’ the market but offered no guarantee of permanency.” (p. 66)

Professor van Aaken’s intriguing and challenging paper goes a good way in laying out the dilemma with which we are faced when designing transnational regulatory regimes. And she is right to imply that we might have to go farther than to utter ‘plus ça change, plus c’est la même chose’. The particular nature of the emerging transnational regimes, which we continue to helplessly refer to as private, quasi-public, or hybrid actors and that are situated in experimental forms of governance, regulation and self-regulation, however, seriously limits our options. In light of the unavailability of either Polanyi’s or the Legal Realists’ return to a deconstruction of market freedoms as political freedoms, the remaining task is to think of ways to translate the institutional and normative underpinning of embeddedness into this new transnational context.

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