Beyond Corporate Governance: Why a New Approach to the Study of Corporate Law is Needed to Address Global Inequality and Economic Development

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Recommended Citation
Danielsen, Dan, "Beyond Corporate Governance: Why a New Approach to the Study of Corporate Law is Needed to Address Global Inequality and Economic Development" (2015). School of Law Faculty Publications. 10.
https://lsr.nellco.org/nusl_faculty/10

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13. Beyond corporate governance: why a new approach to the study of corporate law is needed to address global inequality and economic development

Dan Danielsen

For 40 years or more, corporate law scholars the world over have focused on issues of 'corporate governance' understood as the study of the rules concerning the internal allocation of power and decision-making authority among shareholders and managers in a single firm, and its global corollary 'comparative corporate governance' focused on the impact of domestic corporate governance rules on share ownership patterns in different countries.¹ Scholars of corporate law and development, in turn, have focused on whether there are 'best practice' corporate governance rules that are more conducive to the promotion of national champions, the proliferation of small and medium-sized businesses, or the attraction of foreign direct investment, or the promotion of the productive efficiency of individual domestic firms or that increase the efficiency of domestic capital markets.²

While these issues are important ones, additional areas of inquiry are required to understand the relationships among firms, corporate law and development under current conditions of capitalist production. In particular, we will need to move beyond the study of the internal governance of individual firms and the impact of different corporate law rules on share ownership patterns in two ways. First, we will need to study the institutions and practices that govern relations between firms engaged in geographically dispersed and legally disaggregated networks of value generation, production and distribution, often referred to as 'global commodity chains' or 'global value chains'. Second, we will need to study the ways in which this form of capitalism impacts relations among firms and states as individual firms and the chain as a whole navigate and transform the multiple states, regulators and legal regimes with which they interact in the pursuit of their business objectives. In other words, if corporate law

and development scholars are to contribute meaningfully to theoretical and policy debates about the role of corporate law in fostering economic growth or reducing income inequality, we must take up systemic governance among firms in value chains and broaden our notions of political economy to encompass the multiplicity of firm/state relations that global value chains entail.

In some ways, a shift in the focus of corporate law scholarship to systemic governance among firms and among firms and states would bring scholars of corporate law and development back to the disciplinary preoccupations that drove the study of corporations and corporate law in the late nineteenth and early twentieth centuries. At that time corporate law scholars explored how to facilitate the dynamic potential of large firms to contribute to economic growth and general welfare enhancement while ameliorating the adverse effects of corporate consolidation and power on social and political life — in other words, antitrust (the relations among firms) and political economy (the relation among firms and states). While these issues have remained central to the study of economic development and political economy, they have garnered very little attention within corporate law studies since the 1950s.

Where there are legal scholars who do study corporate power, they are in the field of antitrust or competition law and do so through the lens of corporate consolidation or agreements in restraint of trade. However, the ubiquity in modern capitalism of disaggregated production networks or chains of firms, sometimes related by ownership, but more often by contract, has not been a focus for these scholars. Moreover, the near hegemonic discipline obsession among corporate law scholars, including those concerned with development, with the domestic regulation of individual firm governance and the impact of such governance regulation on public securities markets also misses the significance of global value chains both for development and for firm governance.

To explore how a focus on systemic governance among firms and firm/state relations might be brought to bear in a contemporary context, I consider the recent spate of catastrophic incidents in textile factories in Bangladesh. Well over a thousand workers mostly poor women, have been killed and many more have been injured working in textile factories linked to the global economy through mostly contractual networks of legally independent firms. While the development policy, corporate law and economic circumstances of the Bangladeshi textile industry are in some sense unique, the legal arrangements and institutional forms that link Bangladeshi textile manufacturers to global markets are not. For this reason, I use the events in Bangladesh not as a case study but rather as a conceptual hypothetical for thinking about how the methodological shifts in questions here might enrich corporate law scholarship in general and corporate law and development scholarship in particular.

One reason the traditional corporate law focus on 'best practice' domestic corporate governance rules for domestic firms is problematic is that for many firms in many countries the most important corporate law and business regulation shaping business practice and growth in those countries may not be domestic law.

Let us imagine that most textile factories in Bangladesh are domestically incorporated firms owned by families or family groups or wholly owned subsidiaries of foreign multinational firms. In the case of domestic family businesses, local corporate governance rules would apply to corporate decision making and shareholder protections. With regard to foreign parent companies and their local subsidiaries, decision making with regard to important questions of economic policy, risk management and business conduct would be taken at or directed from the foreign parent level. In such circumstances, the corporate governance rules of the parent's home country would be most important for determining the business practices of the local Bangladesh subsidiary.

While textile firms in Bangladesh (whether owned domestically or by foreign firms) are subject to Bangladeshi labor law, building codes and workplace safety regulations, competitive counter-pressure from foreign multinational purchasers of Bangladeshi textiles and Bangladesh development policy favoring domestic textile manufacturers have encouraged aggressive and dangerous business practices by Bangladeshi factory owners and a culture of bribery and lax enforcement of labor rights and factory building codes by Bangladeshi regulators. These competitive pressures are created in part by major wholesale purchasers of Bangladesh textiles (the H&Ms and the Walmarts and the Gaps and the Carrefours), all firms governed by the corporate law and business regulation of their home jurisdictions and connected to Bangladeshi suppliers via supply contracts, often through multiple subcontractors and intermediaries. To the extent these foreign purchaser firms are concerned with economic or brand risk generated by the business practices of their Bangladeshi suppliers, they may seek to shape those business practices in part through their supply contracts with Bangladeshi firms, with intermediate subcontractor firms or both. In practical terms, this network of contracts may have more impact on the business behavior and practices of Bangladeshi textile firms than the corporate law and the business regulation by the Bangladeshi state. Moreover, the regulatory and enforcement behavior of Bangladeshi public officials may itself be shaped by the business terms set by foreign buyers in supply contacts, on the one hand, and anticipation of the behavior of regulators in competing textile producing states and its effect on the competitive advantage of Bangladeshi suppliers, on the other.

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Thus, even if it were possible to link Bangladeshi corporate governance rules and business regulations to worthy development goals such as enhanced small and medium-sized business development, family entrepreneurship and individual firm profitability through, among other things, wage suppression and low-cost production in the domestic textile industry, the business practices and behavior of Bangladeshi textile firms are also a product of foreign corporate law rules and business practices that even ‘best practice’ domestic corporate law rules would be unlikely to change. For example, even imagining that local Bangladeshi corporate law was an important influence on the operation of some Bangladeshi textile firms, ‘best practice’ fiduciary duty protection for shareholders to police management malfeasance by Bangladeshi managers would be unlikely to induce management to pay greater attention to plant safety or worker protection because the family shareholder beneficiaries of the rules would likely also be the ones setting company policy concerning the working and building conditions in the textile plants. Wage and hour rules or workplace safety standards set in supply contracts may have more effect on Bangladeshi textile firms than national labor or building regulation if the economic risk of losing access to the supply chain of a global purchaser is greater than the cost of non-compliance with Bangladeshi rules.

In sum, business practice, both locally and globally, is to a large extent a function of relations between firms that are themselves subject to the corporate law and business regulation of multiple jurisdictions — conditions that the study of the domestic corporate governance rules and their impact on management and capital structure of individual firms does not begin to capture.

This leads to a second point. Under current conditions of widely geographically dispersed and disaggregated production through loosely, usually contractually related networks of firms, the traditional focus in corporate law and development studies on individual firm governance, domestic firm efficiency and forward and backward linkages among domestic firms may be insufficient to guide the formulation of effective development policy. To the extent that the production and distribution of goods and services globally is organized through global production networks or value chains and the goal of national development policy is to secure and sustain development gains for the national economy, development policy would seem to require at least three considerations in addition to the classical challenges of building the capacity to produce commodities, goods and/or services that can be sold outside the domestic market. First, there is a need to find ways for domestic firms to gain access to relevant global value chains, preferably relatively stable and economically significant ones. Second, policies might be geared to developing legal and institutional mechanisms to manage ‘systemic’ chain governance and ‘systemic efficiency’ rather than, or in addition to, mechanisms that increase efficiency of individual firms. Third, innovation is required to develop strategies for local firms to capture more of the economic surplus from the value chains in which they participate by securing control or dominance over some important aspect of the chain, either through governance techniques or upgrading the role of domestic firms in value creation in chain systems. In such circumstances, the corporate governance issues in question are not, or not only, the legal arrangements for best organizing individual firm governance, but what legal arrangements might be structuring the systemic governance of value chains and whether different legal arrangements might lead to better outcomes with respect to more equitable distribution of gains among firms in the chain, as well as governance tools that might better ameliorate some of the adverse effects of chain production systems — effects such as the dangerous and often deadly conditions for workers in Bangladeshi textile firms.

Looking again to the Bangladesh example, we can see the importance of the study of systemic governance of value chains both for business firms and for development policy planners. Assuming that most Bangladeshi textile firms focused on low-cost production are highly substitutable with one another (and with competitor firms from other low-cost jurisdictions), their bargaining power in relation to the rest of the value chain is likely to be weak. With prices and business terms driven by large foreign buyers, strong competition between Bangladeshi firms for ever-shrinking margins would further weaken the bargaining position of Bangladeshi textile firms. Moreover, to the extent these firms depend on foreign inputs and foreign design as well as foreign branding and foreign marketing, their ability to capture more lucrative parts of the textile/retail chains in which they work and sell would be further limited. Thus, while Bangladeshi textile firms have been able to capture a very large global market share in textile production, the combined business and development strategy of maintaining the market position of low- or lowest-cost producer leaves them with little clout either from a governance perspective or a production perspective to extract more surplus from other players in the global value chains in which they are embedded. In such circumstances, wage suppression, long working hours and poor or unsafe working conditions may be among the few mechanisms through which Bangladeshi textile firms or the Bangladesh state itself can effect profit margins.

For Bangladesh to enhance its ability to extract surplus from its market share in textiles, Bangladeshi firms would need to find ways of taking on more lucrative roles in the value chains systems in which they participate. This goal might be achieved through strategies such as assuming higher-value and higher-skill roles in textile production (design, pattern making, piece production as well as assembly), or attempting to create stronger product differentiation and loyalty among buyers to shift bargaining power in their direction through consolidation with other textile firms in Bangladesh or elsewhere, or asserting some governance or coordinating function, such as certifying compliance by Bangladeshi firms with purchase codes of conduct and/or international labor standards. All of these strategies would require strengthening connections between firm partners in the chain (which likely will not be Bangladeshi firms) rather than creating forward and backward linkages with Bangladeshi firms and suppliers as more traditional development theory might suggest. While the techniques and strategies for obtaining more control over systemic governance of chains and more differentiation and upgrading of the roles for domestic firms in the global value chains will vary from industry to industry and value chain to value chain, it remains the case that all these strategies require a much more sophisticated understanding of the systemic governance mechanisms and business strategies among firms in global production networks — once again, areas of exploration that traditional corporate law and development approaches to corporate governance do not generally study or address.

In addition to inter-firm relations and systemic governance among firms, corporate law and development scholars need a more nuanced account of relations between firms and states. In some sense, this subject has received more attention than the other two I have mentioned, though mainly within a framework of state autonomy and state
capture. While neoliberal development theorists have argued for decades the virtues of a ‘market’ economy driven by private investment, export-led growth and limited state participation (whether through ownership or regulatory action), more heterodox development theorists have asserted that successful development states need sufficient autonomy as regulators to be able to steer private power in the service of national development goals or at least, in the tradition of the Cardoso School of dependent development, to be sufficiently adept at using the limited autonomy they have to secure mutually beneficial bargains with corporate interests. Once again, the Bangladesh example suggests why an approach to governance focused on theorizing the complex relations among states and firms is a necessary component for analyzing the role of firms in development under conditions of modern capitalism.

I have already hinted at a broad range of diverse regimes of corporate governance and business regulation at play in Bangladesh. The tragedy of the collapse of the Rana Plaza factory building killing over 1,100 workers and responses of various corporate actors and industry groups to the tragedy provides a window on some of the complexity of firm/state relations, as well as why corporate law and development scholars need to engage with this complexity if they are to understand or impact the role of firms in development and inequality.

Among large global retailers who were customers of the Bangladeshi factories in Rana Plaza, three main self-regulatory or ‘corporate social responsibility’ responses to the tragedy emerged. Organized by global labor federations and mostly European retailers, the ‘H&M’ (or European) response advocated for providing money to the Bangladeshi factory owners to help fund increased factory safety and to compensate families of injured workers. The Walmart (or American) approach, which rejected the H&M strategy on the grounds that it compensated greedy and unscrupulous factory owners who should bear the costs of factory upgrades, instead proposed using a combination of contract conditionality – requiring suppliers to meet certain labor and safety standards – and inspections conducted or supervised by the big retail partners to enforce the contractual obligations. The final response, the ‘Disney’ approach, involved large companies like Disney pulling their textile manufacturing business out of Bangladesh.

It is worth noting that these diverse responses to the tragic incidents in Bangladeshi textile firms by multinational retailers were not legally required. In fact, the organization of the textile value chain – contractually among legally independent firms rather than through vertically integrated ownership structures of subsidiaries – might have been motivated by an attempt to avoid the very brand risk, oversight responsibility and liability costs undertaken by the lead firm retailers in the aftermath of the tragedies. Rather than legal responsibility, these actions would seem to be the result of market pressure from consumers outraged by the deaths and horrible working conditions of Bangladeshi workers and labor pressure, at least in those European states where more corporatist labor regimes are in operation. At the same time, it was also consumer pressure brought to bear on these same multinational retailers that led them to demand ever higher production quality and quantity at ever lower cost from their Bangladeshi suppliers. That pressure, in turn, led to the lack of labor law and building code enforcement by the Bangladeshi state and the price competition among Bangladeshi factories and other potential low-cost suppliers that, in turn, may have led to unscrupulous business practices of the owners of the textile factories in Bangladesh. In other words, consumer outrage over unconscionable wages and working conditions pushed in the direction of a corporate social responsibility agenda while consumer demand for constantly new fashions at bargain basement prices undermined efforts to achieve higher wages and better working conditions in the factories. The point is not to shift responsibility for working conditions in Bangladesh from firms to consumers, but rather to suggest that the dynamics and pressures among and within firms and among consumers who are not all able or willing to make purchasing decisions on ethical, as opposed to price, grounds are much more complex than they might at first appear.

The Bangladeshi state reacted to the private initiatives by large retailers with promises of increased enforcement of its building codes and revisions to its labor laws, in principle to facilitate worker organizing and collective bargaining, though many NGOs and labor organizations analyzing the reforms have suggested that the regulatory revisions did very little to change the status quo for textile workers in Bangladesh and in some cases made things worse. One challenge for Bangladesh with respect to labor reform is the fact that improving labor conditions through increased safety and building regulations would seem to work at cross-purposes with Bangladesh development policy of retaining low-cost producer advantage in textiles. Add to that market pressure from other states competing for business from large foreign buyers of low-cost textiles in part through suppression of labor rights and costs. Finally, Bangladesh faces political challenge of resisting the power of the now entrenched textile factory owner elites created in part through the success of Bangladesh’s industrialization strategy focused on textile production. In a certain sense then, the cross-cutting pressures on the Bangladeshi state that might undermine its will or ability to improve labor conditions in textile factories are similar to the bidirectional forces of consumer pressure on firms...
both toward and away from corporate responsibility for labor conditions in global textile value chains.\(^\text{14}\)

To complicate matters further, at the transnational level, the United States suspended its special tariff treatment of Bangladeshi textiles under the Generalized System of Preferences due to Bangladesh’s failure to enforce internationally recognized labor rights and protections and the EU threatened to follow suit.\(^\text{15}\) Meanwhile, US government procurement policy requires ‘lowest cost suppliers’ resulting in significant price pressure on and purchases from the very same Bangladeshi textile suppliers, even as the US government chastises the Bangladeshi state for its labor practices.\(^\text{16}\)

In such complex circumstances, the paradigm of state capture and state autonomy is simply inadequate to the task of either describing or resolving the play of forces or actors responsible for working conditions in Bangladeshi textile factories. Moreover, even if the deadly working conditions are conceived as some type of regulatory failure, it is very difficult to tell whose failure. Who is being regulated by whom and how? What is public and what is private regulation, or what is local and what is global regulation? It might be comforting to assume that the circumstances at work in Bangladesh are unique, but my argument is that the complexity and ambiguity evidenced by the multiple regimes and political and economic forces shaping production, consumption and distribution of Bangladeshi textiles is not exceptional. Rather, the Bangladesh I am narrating here provides a window for seeing what we face in understanding and theorizing the structure and operation of the global economic and regulatory order in general.

To take this one step further, continued fealty to a conception of the global order — premised on effective ‘public’ and largely national oversight of autonomous economic actors operating in a largely ‘private’ economic sphere that provides the often unstated anchor for scholars of corporate law and governance in the traditional mode — is neither helpful as a description of the global system nor useful as a model for explaining the ever-increasing asymmetries in the distribution of power and resources among and between states, firms and people across the developed and developing worlds. The notion that each nation state bears the individual sovereign responsibility for both facilitating the gains and controlling the excesses of self-interested private economic actors within its jurisdiction obscures the radical asymmetries in power, capacity and resources among states, regulatory institutions and firms that frequently shape and sometimes determine regulatory and distributional outcomes both in individual states and across the global system.

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In short, if scholars of corporate law and development are going to be relevant analyzing conditions of underdevelopment and gross inequality so prevalent in the global system, they will need to develop new and much more complex accounts of the role of law in shaping the structure and governance of global value chains, on the one hand, and the role of value chains in shaping the dynamic relations among firms and states in the global economy, on the other.

Seen through the lens of traditional corporate law, a ‘global value chain’ would consist of a disaggregated network of independent corporate entities of diverse scale and geographic location connected and coordinated primarily by contract. Yet, in years past (and perhaps again in the future), the production and distribution functions that the modern global value chain is designed to accomplish might have been accomplished through vertical integration of all or the vast bulk of the design, production and distribution processes in a multinational corporate firm organized and controlled through ownership. Without conceding legal liability of parties up the value chain, the various industry responses to the Rana Plaza and other disasters in textile factories in Bangladesh have suggested a conception on the part of lead firms of some joint responsibility for the actions of legally independent but nevertheless interdependent entities in the value chain. Perhaps this sense of shared responsibility for the value chain is evidence of a shifting conception of the ‘firm’. Perhaps a notion of value chain as ‘firm’ is a conception in need of exploration – the ‘nexus of contracts’ our law and economics colleagues use to describe the single corporation, writ large and in global terms.

From the standpoint of corporate law and governance, it may be the case that improving the conditions of work, industrialization and economic growth that enable Bangladeshi industry to participate in the global economy and global consumers to benefit from low-cost textiles will require a corporate law aimed at shaping the behavior of the value chain itself as ‘firm’ or ‘system’ rather than assuming that attention to the corporate governance of individual corporations will lead to improved development and governance at the global level. From the perspective of legal accountability, the notion of enterprise liability is not new, at least with respect to multinational conglomerates whose constituent firms are linked by ownership. But exploring the social welfare or development effects of enterprise liability based on functional interdependence, regardless of whether such interdependence is coordinated via ownership or contract, becomes much harder even as a thought experiment if corporate law and development scholars take as given the legal independence and limited liability of separately incorporated business entities.

Corporate law and development scholars might begin to engage the diverse and complex range of relations among firms and states by attempting to theorize the global economic and regulatory order in actual operation rather than the one we might conventionally expect to find — national public order and independent private firms. The global order that emerges from the Bangladesh story looks more like a dynamic, continuous and cumulative co-production of states and firms with different baseline allocations of power, resources and capacities, bargaining over, making, adapting and resisting the rules of the game, on the one hand, and anticipating, making and reacting to assertions of power by players in the system, on the other. A focus on global value chains and the numerous states and regulatory systems with which they interact, as well
as the regulatory systems and governance structures these value chains produce, might help to bring some order to the unwieldy and chaotic complexity of firm/state relations in operation on a global scale. Seeing the global order as a dynamic system in perpetual production, itself defining and redefining the boundaries among public and private, governors and governed, and legitimate and illegitimate assertions of authority, invites us to shift the focus of study in corporate law and development from how to produce and maintain an appropriate (if not always optimal) balance between 'public' order and 'private' initiative to how to re-imagine the meaning and potential of regulation in circumstances where state and firm, public and private, governor and governed blur and blend in ways that belies simple narratives of autonomy and capture.

It may be that such an exploration will undermine our confidence in the potential of the 'development state' and national development policy to influence this complex regime of firm/state governance. It may turn out that neither the Bangladeshi state nor the world's largest retail firms can resolve on their own the contradictions and challenges of growth and deprivation at work in the textile mills of Bangladesh and the department stores of the Global North. At the same time, as we shift from a focus on domestic corporate governance of individual firms and nation state responsibility for the regulation of private firms within their borders to notions of systemic governance across firms and states and collective responsibility for the adverse consequences of the state/firm configurations that comprise modern value chain capitalism, new sites and legal mechanisms should emerge for intervention in the service of more equitable distribution of the surplus within chains and more effective allocation of responsibility and authority among chain actors. By tracing dynamic processes of cumulative causation and systemic patterns of interdependence, shifting advantage, adaptation and crisis among players in the global system, regardless of their more conventional designations as public authorities or private actors, domestic or foreign, we should be better able to discern both the legal mechanisms through which power and resources are distributed among chain actors and to identify the mechanisms most likely to enable the reallocation of power and resources in more equitable and less damaging ways. In this conception, as in its early iterations, corporate governance becomes once again a mechanism for the study of institutional form, economic power and social welfare – issues central to discerning pathways to equitable development and human flourishing. In other words, issues that matter.