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Transnational Corporations and Public Accountability

THE ROLE OF TRANSNATIONAL CORPORATIONS (TNCS) IN THE GLOBAL economy has increased considerably during the second half of the twentieth century. Their activities have grown at a much faster pace than world output, and during the 1990s the stock of foreign direct investment (FDI) has almost quadrupled, from $1.7 trillion in 1990 to $6.6 trillion in 2001. UNCTAD estimates that today there are about 64,000 TNCS, with about 840,000 foreign affiliates. These affiliates account for about 54 million employees, but the economic importance of international production is even higher when non-equity relationships such as subcontracting and licensing are considered.

What TNCS do (or do not do) affects the lives of a substantial share of the world’s population. This impact can take many forms: for instance, the dissemination of new technologies and management practices changes production methods and performances of domestic industries; extractive activities can change the lives of local communities and local affiliates of TNCS can be agents of cultural change in host societies. Because of their size and capacity to transcend national boundaries, TNCS have traditionally been a reason for concern on the part of important social and political groups, notably trade unions and socialist, traditionalist and nationalist parties. The governments of recently de-colonized countries perceived TNCS as potential or actual agents of a neo-colonialist project aiming at exploiting national resources without adequate compensation and at interfering in the political process of the newly independent states.

1 I am grateful to Daniele Archibugi and David Held for their comments on previous drafts. I am responsible for any mistake. The financial support of the Rockefeller Foundation is gratefully acknowledged.

During the 1990s, the economic and political significance of TNCs has brought them once again into the spotlight of public attention. Anti-corporate activism has become a mass movement again, with campaigners forming networks at the same global level as the activities of the TNCs they target. This is a serious challenge for TNCs, since it may trigger a reversal of the trend towards a business-friendly political climate that has dominated policy-making in developed and developing countries since the early 1980s.

At the heart of this challenge is the issue of accountability. Because of their often huge economic clout and their capacity for global mobility, corporations are widely perceived as capable of evading public control and getting away with behaviour that harms employees, consumers, vulnerable communities or the environment. ‘Economic globalization’ is considered responsible for altering the balance of power between citizens and corporations in favour of the latter, thus reversing in part the achievements of the struggles for the democratization of national politics and societies in developed countries and for national self-determination in the developing world. ‘Globalization means that it is more difficult for national governments to hold corporations accountable than in the past.’

This article considers the issue of public accountability of TNCs in the light of the experiences of the past 30 years. The next section discusses briefly the problem of accountability of corporations in general. The second section examines the accountability gaps that are particularly severe as a result of the transnational reach of TNCs. The third section looks at existing attempts to close these gaps, including intergovernmental cooperation, business ‘self-regulation’ and initiatives that involve nongovernmental organizations and supranational agencies in defining standards of conduct for companies and monitoring their compliance; it will also try to assess to what extent these initiatives are able to close the accountability gaps generated by transnationalized production.

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CORPORATIONS: HOW ARE THEY ACCOUNTABLE TO WHOM FOR WHAT?

Most generally, ‘an accountability relationship is one in which an individual, group or other entity makes demands on an agent to report on his or her activities, and has the ability to impose costs on the agent’. Somewhat more specifically, accountability is frequently defined as applying to situations in which an agent ‘is held to answer for performance that involves some delegation of authority to act’. Directors of corporations are certainly meant to be accountable in this sense, since their authority in the organization is the result of a formal act of delegation by the shareholders. It might be less obvious why corporations should be accountable to the general public, since no delegation of authority seems to occur between them. However, the granting of charters and legal personality to collective financial entities by the state was prompted at least in part by the benefits that the separation of personal finances and business finances were expected to bring to the broader public, especially in relation to major ventures, such as the opening of new commercial trade routes, the building of railways and ships, and large industrial projects. Corporations are not ‘natural entities’, but creatures of legislation. The idea that corporations should have a special duty of accountability to the wider public is therefore justified in light of their owners’ enjoyment of limited liability.

In addition, influential strands in democratic theory hold that delegation of authority is not the only reason why one actor can legitimately demand accountability from another actor. The fact that a person or community is substantially affected by the actions of an individual or organization may, under certain circumstances, justify the establishment of a relationship of accountability between them. In the words of Robert Keohane, ‘internal accountability’ to those

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4 Ibid., p. 139.
who delegate power to and support an agent may be insufficient and need to be complemented by mechanisms of ‘external accountability’ to the wider circle of persons who are affected by the agent’s decisions and actions. Because of their central role in modern economies, corporations are prime targets for demands for increased public accountability. In the national context, the social groups formulating these demands have been mainly the labour movement, consumers’ associations, women’s movements, environmentalists, and sometimes the general public, especially after dramatic events and accidents. As a result of these various demands, in the national contexts corporations are typically involved in a complex set of accountability relationships.

Accountable to whom? – Corporations are variously accountable to their owners, creditors, employees, customers, other corporations (through business associations) and to the general public through state institutions – legislatures, bureaucracies and courts. Internal accountability, as defined by Keohane, is usually stronger than external accountability, and within companies the accountability to shareholders is stronger than accountability to other groups with institutionalized relationships to the executive directors, notably the employees.8 However, even the strength of internal accountability should not be overestimated. Susan Strange notes that ‘The multiple accountability of CEOs to shareholders, banks, employees, suppliers and distributors, not to mention strategic allies, means that like renaissance Princes, they can usually divide and rule.’9

How are they accountable? – Mechanisms of accountability vary, but two aspects are crucial to all accountability relationships: the flow of information to the principals and other stakeholders about the decision-makers’ actions, and the capacity of stakeholders to impose

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8 Indeed, for many democratic theorists the main accountability deficit afflicting the large corporation is the insufficient accountability of managers towards the employees. See, for instance, Robert Dahl, *A Preface to Economic Democracy*, Berkeley and Los Angeles, University of California Press, 1985.

sanctions on the agents. On the one hand, stakeholders must possess certain types of information (provided by the agent or third parties such as external auditors or ‘watchdog’ associations) to exercise accountability, notably information about formal decision-making procedures, actual decision-making processes, various outputs (including compliance with regulations, financial management, etc.), the outcomes expected by decision-makers and the actual outcomes of the activities of the organization. On the other hand, stakeholders must be able to punish decision-makers if their performance is unsatisfactory. Depending on the kind of stakeholder/principal and on the circumstances, this punishment can consist of removal from the job, reduction of powers and competences (i.e. redefinition of mandate), withdrawal/non-renewal of the licence to operate, termination of financial support or service provision, infliction of financial penalties (e.g., tort law), loss of reputation and prestige, loss of customers and market share, or criminal prosecution.

Accountable for what? – Different categories of principals may have different goals, and a principal might want the agent to pursue several goals at the same time. For instance, shareholders might want directors to increase dividends and refrain from ‘unethical’ investments, the employees might want to be given high salaries and pleasant working conditions, and so on. Similarly, state institutions hold companies accountable for their compliance with a diverse range of regulations. These regulations aim to protect various stakeholders: investors and creditors (accounting practices and financial probity), workers (minimum wage, trade union organization, health and safety in the workplace), consumers (competition laws, product safety, particularly regarding food and drugs) and the public at large (environmental, tax and criminal law).

TRANSNATIONAL CORPORATIONS AND ACCOUNTABILITY GAPS

Companies are accountable to the general public mainly through the governments of the countries where the companies conduct their

This corresponds to the assumption, common to most democratic thought of the nineteenth and twentieth century, that the relationship between political decision-makers and the recipients of political decisions is ‘symmetrical’ and ‘congruent’.11 This assumption may be justified to most activities of most companies. However, it can become quite problematic in the case of TNCs. The congruence between the two sides of the accountability relationship can be put into question by the mismatch between the growing integration of world markets and the fragmented character of world politics. The globalization of economic activity breeds the potential for ‘accountability gaps’12 that would not occur, or be less severe, in a world of closed economies.

Pointing at accountability gaps does not imply that TNCs should be thought of as ‘footloose’ entities that are able to evade any constraint. The ability to withhold territorial access remains a crucial resource of states in dealing with TNCs and other transnational actors.13 However, transnationalized production challenges the standard model of public accountability of corporations through governmental regulation and supervision. Broadly speaking, there are four sources of accountability gaps in the relationship between TNCs and citizenries: the collusion between government officials and the directors of TNCs; the consequences of regulatory competition; the problem of weak and collapsed states; and subversive activities by TNCs.

Collusion Between Government Officials and Transnational Corporations

Collusive behaviour can range from relatively benign forms, such as the provision of campaign money in exchange for privileged access to decision-making, to severe forms of corruption that distort sub-

stantially the political process and its outcomes. Certainly, collusion between public officials and business is not unique to the relationship between TNCs and host governments – also domestic companies engage in collusive practices. But collusion involving TNCs, especially with authoritarian governments in developing countries, may have an particularly detrimental effect on the prospects of effective mechanisms of accountability.

Several commentators are concerned that TNCs are attracted by countries in which democratic rights are curtailed, and that their presence in the country prolongs authoritarian rule.\(^\text{14}\) While it is true that wages tend to be lower under authoritarian regimes than they are in democratic countries,\(^\text{15}\) the evidence suggests that, on the whole, democratic political systems tend to attract more FDI inflows than their authoritarian counterparts.\(^\text{16}\) But this certainly does not rule out that in specific situations, the collaboration between a government and a TNC makes the latter less accountable to the citizens of the host country. The risk of harmful collusion is especially strong with regard to companies that extract natural resources in developing countries.\(^\text{17}\) In this sector more than others, TNCs may take investment decisions with little regard to the vital interests of local communities and at the same time provide the government with resources – royalties and tax revenues – that are vital for maintaining the political status quo. During the 1990s, Shell came under intense pressure to review its collaboration with the Nigerian government, in the light of severe human rights abuses linked to its use

\(^{14}\) Keohane and Ooms remarked that foreign investment has a right-wing bias and that under some circumstances it may ‘bolster the position of a government, strengthening its support among key elites and reducing the necessity to satisfy nonelite demands’ Robert O. Keohane and Van Doorn Ooms, ‘The Multinational Firm and International Regulation’, *International Organization*, 29: 1 (1975), pp. 169–209; 180.


of Nigeria’s oil resources.\textsuperscript{18} In the 1980s, stopping foreign investment in South Africa was seen by anti-apartheid activists as an important means for pressing the government towards political reforms.\textsuperscript{19}

\textit{Regulatory Competition}

Until the 1970s, the governments of developing countries had an ambivalent attitude towards foreign investment. The concern was that, left to themselves, TNCs might exploit the resources of the host countries without giving much in return. Foreign investment was thus subject to a wide range of restrictions and requirements related to profit repatriation, technology transfer, exports, domestic participation, the local content of products and other aspects of TNC activity.\textsuperscript{20} This has changed in the meantime and today most governments accept that it is not in their interest to exclude their countries from access to global technologies and global markets – and consequently from the TNCs that facilitate this access.\textsuperscript{21} The prevailing view is that FDI is beneficial to developing countries,\textsuperscript{22} and most of them have enacted regulatory changes aimed at attracting foreign capital.

\begin{itemize}
\item \textsuperscript{22} Econometric studies suggest that FDI inflows contribute to long-term economic growth. Robert E. Lipsey, ‘Inward FDI and Economic Growth in Developing Countries’, \textit{Transnational Corporations}, 9: 1 (2000), pp. 67–95; Eduardo Borensztein, Jose De Gregorio and Jong-Wha Lee, ‘How Does Foreign Direct Investment Affect Economic Growth?’, \textit{Journal of International Economics}, 45 (1998), pp. 115–35. These studies also suggest that the impact of FDI on growth is marginal in countries with low levels of education, but becomes stronger as the level of schooling increases.
\end{itemize}
The ability of multinational corporations to choose in which jurisdiction to locate their activities, however, affects the capacity of governments to hold them accountable for their social, environmental and fiscal performance. Internationally mobile capital is a scarce good, and governments have incentives to engage in competition for investment by lowering taxation and social and environmental standards or by refraining from enforcing the standards that formally exist. Regulatory competition impairs the accountability relationship between governments and TNCs, since it induces the principal to relax its demands on the agent and to abstain from punishment for fear that the agent will move to the jurisdiction of another principal. In a sense, the TNCs’ opportunities for ‘exit’ turn the accountability relationship upside down by making governments accountable to TNCs, or at least by increasing the bargaining power of TNCs vis-à-vis the governments.

An extreme interpretation of these developments holds that ‘not much remains of the accountability of market forces to political constraints’. But this view underestimates some important resources held by governments. First, once foreign investment decisions are implemented, reversing them is often costly for companies, and governments have additional means to ‘lock’ them in – the extreme case being expropriation. Through their power over territory, states can control investment flows. Second, governments control resources – infrastructures, human capital, legal systems, natural resources, etc.

23 From the perspective of countries, capital has strong characteristics of a common pool resource, i.e. it is rival in consumption and non-excludable. This should make ‘competitive extraction’ the dominant mode of appropriation. See Alkuin Kölliker, ‘Competing for International Economic Commons: Towards a Collective Goods Theory of Regulatory Competition’, paper presented at the ECPR Joint Sessions, Edinburgh, 28 March–2 April 2003.

24 Strange, The Retreat of the State, op. cit., p. 197.

25 Indeed, expropriation and nationalization were a common risk associated with foreign investment, especially in Latin America and in oil-exporting countries. See Vernon, In the Hurricane’s Eye, op. cit.

26 Geoffrey Garrett, ‘The Causes of Globalization’, Comparative Political Studies, 33: 6/7 (2000), pp. 941–91. But the importance of this factor for the bargaining power of states depends to a large extent on what is produced (e.g., mining, garments, banking): ‘If production can take place in any one of a number of countries, the ability to grant entry to any one country will not be worth much’. Krasner, ‘Power Politics, Institutions and Transnational Relations’, op. cit., p. 275.

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that companies need for their activities and that are not easily reproduced.27

The available evidence seems to indicate that, on the whole, OECD countries are able to resist the downward pressure of competitive regulation.28 But fiscal, social and environmental ‘races to the bottom’ are a serious risk in the developing world. The picture is mixed. For instance, sometimes TNCs bring advanced environmental processes to their foreign plants even when host countries do not mandate them.29 But in other cases TNC choose production locations with an eye to taking advantage of lax environmental regulation and enforcement, with governments of host countries ‘occasionally pointing to the feebleness of their environmental regulations as a selling point in initially attracting them’.30 Even though a ‘pollution haven’ strategy may be unable to attract large amounts of inward investment, dramatic episodes such as the Bhopal catastrophe show the risk involved in lax standards and enforcement.31 Also tax policies are affected, since governments offer subsidies and tax exemptions to TNCs for the sake of job creation and technology transfer,32 while the mere threat of exit allows them to elicit concessions from their host governments.33 In most cases, ‘the perception of more mobile production may be more important than the actual behaviour of business’.34


30 Vernon, *In the Hurricane’s Eye*, op. cit., p. 58.

31 Hansen, ‘Environmental Regulation of Transnational Corporations’, op. cit., p. 171. In 1984 an accident at a subsidiary of the US company Union Carbide killed several thousand people in Bhopal, India.


33 Ibid., p. 39. Moreover, through transfer pricing, companies are able to move their global profits to less demanding jurisdictions. Similarly, they can protect shareholders from liability in different countries by creating separate legal entities.


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State Weakness and Breakdown

Host governments might be unable to act effectively as agents of accountability between TNCs and citizens because of the lack of material and organizational resources for policy formulation and implementation. Often the problem is limited to the possession of inadequate administrative and technical capabilities. For instance, transnational food corporations have exploited the weaknesses of public health systems in some developing countries to engage in dangerous marketing practices of breast-milk substitutes. But sometimes the problem emerges in an extreme form when countries are affected by large-scale violence and civil war. While most multinational corporations have no interest in entering or remaining in these countries, a few companies may have reason to stay and take advantage of the situation. In recent years, the case of multinational corporations trading in rough diamonds and minerals in Congo and other conflict zones has been particularly prominent. Corporations might collude with one of the conflict parties and prolong the conflict as a result of their financial support. In some cases, corporations may fuel the conflict directly by providing arms to the fighting parties. Under these conditions, any normal relationship of accountability breaks down.

Political Subversion

Finally, TNCs may try to avoid public accountability by promoting the overthrow of the government that is supposed to hold them


accountable. Such actions are comparatively rare, but episodes such as the involvement of the United Fruit Company in the Guatemalan coup d’état of 1954 and ITT’s machinations against Salvador Allende’s government in Chile contributed to the widespread perception of TNCs as a potential threat to national sovereignty and democracy. Like the other sources of potential accountability gaps, this risk is more serious in developing countries than in developed countries.

GLOBALIZED ACCOUNTABILITY MECHANISMS

Since the activities of TNCs span several jurisdictions, they have more opportunities to evade demands for accountability or to engage in collusive behaviour with unaccountable governments than other organizations. This is made easier by their sheer economic size. In principle, governments are able to impose substantial restrictions on the mobility of companies, but this could involve considerable economic and social costs and ultimately not bring an improvement in the citizen’s ability to hold decision-makers accountable. The accountability gaps brought about by TNCs are all the more serious as trade unions, which in industrialized countries have traditionally been the main countervailing power to business interests, find it difficult to cooperate effectively with one another at the transnational level.

This section presents an overview of the attempts, initiated by governments, international organizations, nongovernmental organizations (NGOs), advocacy groups and business groups themselves, to establish mechanisms of accountability that would operate at the same global scale as the activities of TNCs. A crucial distinction is that between mandatory and voluntary mechanisms. A fully mandatory mechanism operates in the same way as national legislation: it sets precise rules of conduct, creates obligation and creates mecha-

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nisms for adjudication and enforcement.40 Some forms of international regulation might consist of ‘softer’ rather than ‘hard’ law, but they could still be considered mandatory. By adhering to voluntary mechanisms of accountability, on the other hand, companies commit themselves to disclose their activities and thus make it easier for consumers, investors and other stakeholders to assess their social and environmental performance and make their choices accordingly. In voluntary mechanisms, sanctions are essentially informal and decentralized. Also voluntary mechanisms are a matter of degree: independent institutions that formulate the rules that may be adopted by companies, monitor their compliance and report violations of commitments to the public all reduce the ‘voluntarism’ of standard-setting and certification. The distinction between mandatory and voluntary is best thought of not as a dichotomy, but as the ends of a continuum displaying decreasing degrees of corporate discretion.

The trend of transnational accountability mechanisms has to some extent mirrored the changes in national regulatory environments. In most countries, heavy regulation until the 1970s has been supplanted by deregulatory policies during the 1980s. Similarly, the emphasis of the international debate in the 1970s was mainly on the creation of mandatory frameworks for TNC regulation, whereas the debates of the 1980s and 1990s were mostly about corporate self-regulation. More recently, co-regulation through multi-stakeholder partnerships has received much attention.

Intergovernmental Cooperation

Unlike trade and finance, multinational corporations and foreign investment are not governed by a coherent international regime.41 This absence is due mainly to a fundamental disagreement about the prime objective of such a regime: should it protect foreign investment from discriminatory policies of governments, or should it curb the power of multinational corporations for the sake of national


41 Held et al., *Global Transformations*, op. cit., p. 257. See also Keohane and Ooms, ‘The Multinational Firm’, op. cit.
economic sovereignty? This question prevented the emergence of a comprehensive global regulatory framework for over 30 years.\textsuperscript{42} It is notable that this outcome was not intended by the architects of the international economic order after the Second World War. The Havana Charter granted to the International Trade Organization some competences over the policies of governments towards TNCs as well as the conduct of TNCs themselves. What is remarkable is that the provisions concerning host-nation policies were weaker than those regulating restrictive business practices on part of TNCs. This asymmetry was due to concerns about restrictive practices, and specifically about international cartels, that stemmed from the inter-war experience. The opposition of business actors to these provisions was a contributing factor in the failed ratification of the charter.\textsuperscript{43}

The debate about international regulation of TNCs resurfaced in the late 1960s. Developing countries requested the adoption of an international code of conduct for TNCs, whereas most developed countries were either opposed or indifferent. The aims of the developing country governments were economic (the increase of their bargaining power vis-à-vis foreign investors) as well as political (the prevention of anti-governmental activities by TNCs). A few international arrangements emerged from these debates: the United Nations set up a Centre on Transnational Corporations (UNCTC), which drafted a code of conduct for TNCs in 1978 and revised it in later years (the code was never adopted); the OECD issued a set of Guidelines for Multinational Enterprises in 1976; the International Labour Organization (ILO) issued the Tripartite Declaration of Principles Concerning Multinational Enterprises and Social Policy in 1977; UNCTAD formulated a code on restrictive business practices and a code on technology transfer, which were adopted by the UN General Assembly in 1980. None of these initiatives was of much consequence to the actual regulation of TNCs.

The efforts of developing countries to establish international rules for TNCs subsided in the 1980s, as a result of their changed attitude towards foreign investment. Almost all of them altered their public


policies so as to attract rather than control foreign investment.\textsuperscript{44} The great majority of regulatory reforms aimed at making the domestic investment climate more favourable to inward FDI.\textsuperscript{45} Similarly, negotiations on international arrangements regarding investment continued throughout the 1990s, but these aimed at providing a framework for the liberalization of investment rules and mechanisms for investor protection rather than putting constraints on TNCs. This was evident in the Multilateral Agreement on Investment (MAI) negotiated at the OECD and in the discussions within the GATT/WTO context.\textsuperscript{46} While several global intergovernmental agreements regulate specific aspects of foreign investment,\textsuperscript{47} regional arrangements (NAFTA, EU) and bilateral treaties are still the main source of rules and standards on international investment. Governments that accede to these multilateral and bilateral agreements limit their own freedom of action with regard to foreign investors and thus may reduce their capacity to hold corporations accountable in specific circumstances.

International regulation of TNCs is less developed than norms about foreign investor protection and property rights. Environmental NGOs tried to include strong norms about TNC

\textsuperscript{44} Vernon, \textit{In the Hurricane’s Eye}, op. cit., p. 31.

\textsuperscript{45} See the annual overviews in the World Investment Reports issued by UNCTAD.


\textsuperscript{47} Tolentino, ‘Transnational Rules’, op. cit., lists 27 intergovernmental instruments concerning TNCs adopted between 1948 and 1998. The UN estimates that at least 35 international regulatory instruments, such as the Basle Convention on hazardous waste to the Montreal Protocol on ozone-depleting substances, constrain the activities of TNCs; but the effectiveness of international environmental law vis-à-vis TNCs is limited by its fragmented character and by the failure of many host countries to ratify the relevant agreements. Hansen, ‘Environmental Regulation of Transnational Corporations’, op. cit., pp. 172 and 183, n. 12. With regard to labour and other human rights, the (limited) role of the UN agencies in holding corporations accountable is reviewed by David P. Forsythe, \textit{The Political Economy of Human Rights: Transnational Corporations}, Human Rights Working Papers, 2001, available at http://www.du.edu/humanrights/workingpapers/index.html.
responsibilities for sustainable development in the final documents of the 1992 UN Conference on Environment and Development in Rio de Janeiro, but their efforts were largely unsuccessful, not least because of the major role of the Business Council for Sustainable Development in shaping the chapter on business in Agenda 21.48 Business groups succeeded in presenting self-regulation as an effective alternative to ‘command-and-control’ approaches. After Rio, some NGOs and transnational advocacy networks continued to consider mandatory regulation as the only effective way to hold companies accountable for their environmental performance, but an increasing number of NGOs were willing to engage with companies and help shift the self-regulatory trend towards forms of ‘multi-stakeholder’ co-regulation.49

Intergovernmental regulation of TNCs was hindered by conflicts of interest between states. The history of the attempts at creating an intergovernmental regulatory framework for TNCs essentially confirms a hypothesis formulated by Keohane and Ooms almost 30 years ago: ‘We can only expect extensive international regulation on a global scale where the principal issues pit the state against the enterprise, rather than state against state with the enterprise only as a willing or unwilling intermediary’.50

Voluntary Mechanisms

In the past few years, an increasing number of TNCs decided to participate in voluntary institutions designed to enhance their public accountability. These decisions resulted from a number of considerations, whose weight depended on the circumstances. The most common reasons for action were: the concern that the business might lose customers and investors as a consequence of negative pub-
licity; the hope to gain new customers and investors by projecting an image of corporate responsibility; the prevention of court litigation; the prevention of state regulation; and the improvement of the morale and loyalty of employees. In general, corporations whose reputation is at risk because of the activities of consumer and advocacy groups may prefer to submit to institutionalized mechanisms of accountability rather than to be exposed to unpredictable and uncontrollable punishment in the marketplace. Moreover, an important incentive is the prevention of more stringent national and international regulation, especially in the wake of major disasters such as the Chernobyl accident in 1986 and Exxon Valdez oil spill in 1989.51

Voluntary mechanisms are mostly based on communicating to interested parties that the firm complies with certain procedural or substantive standards of conduct. This involves two steps.52 In the first step, the standards must be formulated and made public. There are essentially three types of standards:53 1) process standards, which specify procedural rules such as the establishment of management systems and platforms for stakeholder consultation; 2) performance standards, which specify what companies should do or not do; and 3) certification standards, which define how compliance with process and performance standards should be monitored and certified. The second step consists in certifying that a company complies with the standards. Certification can involve several activities: internal audits, annual reports of social and environmental performance, third-party inspections and auditing, and verification (when an independent authority re-examines a prior monitoring activity).

Standards can be set internally by each company, collectively by the corporations of a certain industry or economic sector, or by external third-party entities. Similarly, compliance can be certified through a purely internal audit process (self-certification), by industry associations, or by external monitoring and certification agents. Different combinations of these functions are possible: for instance,

53 See Malcolm McIntosh, Ruth Thomas, Deborah Leipziger and Gill Coleman, Living Corporate Citizenship, Harlow, FT Prentice Hall, 2003. These authors add foundation standards to this list.
standards may be set by an individual company but certification might be conducted by a third party.\textsuperscript{54}

\textit{Internal standards and certification}. – Many TNCs have adopted company codes of conduct and/or publish reports on their social and environmental performance in addition to their financial reporting.\textsuperscript{55} In the case of exclusively internal standard-setting and certification, companies decide the norms to be incorporated in their codes of conduct, and compliance with those rules is monitored through internal procedures. Essentially, companies ask interested parties to trust the adequacy and accuracy of these internal rule-making and monitoring procedures. From the point of view of public accountability, purely internal certification raises two problems. The first problem is that unilateral codes frequently ignore key concerns of stakeholders,\textsuperscript{56} moreover, even those directly affected (such as workers) often do not know how to use the code to the express complaints.\textsuperscript{57} The second problem is that self-certification is usually not sufficient to provide reliable information about compliance when, on balance, deception or lax enforcement would be advantageous to the firm.\textsuperscript{58} Considering also that many companies – especially smaller companies\textsuperscript{59} – are not interested in adopting codes of conduct,

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company codes of conduct have serious deficiencies as mechanisms of accountability.

_Sectoral standards and certification._ – In some cases, projecting an image of high standards and accountability can be a source of competitive advantage for corporations. Most of the time, however, standards are mainly a source of costs for the companies that actually implement them, and thus compliant companies are interested in levelling the playing field by extending standards to other companies in the same industry. Moreover, what one company does may affect the reputation of other companies in the same industry. High-standard companies are thus likely to promote the creation and enforcement of sector-wide codes of conduct. But such codes also can be useful to other companies in the sector because they can reduce uncertainty about which rules and regulations should be followed and increase the information about what other companies in the sector are doing.

Sectoral codes of conduct are common especially in sectors where the risk of damaging the collective reputation of the whole industry is especially high. This can be a consequence of the inherent risks associated with the industry’s operations, as in the case of the World Association of Nuclear Operators, the Responsible Care programme of the chemical industry, and the Guidelines for Good Manufacturing Practice of the pharmaceutical industry; or it can be a consequence of the vulnerability to negative reactions by consumers, which persuaded industry groups such as the World Federation of Sporting Goods Industry and the British Toy and Hobby Association to develop codes of conduct for their associated companies. Similarly, the diamond industry has reacted to campaigns about ‘blood diamonds’ from conflict zones by creating a World Diamond Council that developed a code of conduct for its members. Also the International Federation of Organic Agriculture Movements (IFOAM) exercises a form of collective self-regulation.

From the point of view of public accountability, sectoral codes are an improvement on company codes, but are not without their

problems. Hansen has pointed at the crucial problem of inclusiveness: ‘Standards and guidelines such as the ICC Business Charter for Sustainable Development or the environmental management standards issued by the ISO are, for all practical purposes, initiated, drafted and adopted by OECD-based companies for OECD-based companies. LDCs [less developed countries], consumer groups and environmental NGOs have little influence on these activities.’62 Another problem is that ‘industry associations are reluctant to punish noncomplying members or make public their violations’.63 A systematic evaluation of the Responsible Care initiative suggests that any programme without third-party monitoring and sanctions for non-compliance is likely to be ineffective.64 Sectoral codes are not really able to assuage concerns about the performance of TNCs, pointing to the inherent limitations of mechanisms of accountability that are designed and managed by business actors themselves.

External standards and certification. – Collaborating with other companies in the same sector solves some of the credibility problems of unilateral codes and reporting, since sectoral associations can exercise a degree of surveillance to prevent damages to the collective reputation of the industry. But neither the formulation nor the monitoring of sectoral codes is truly independent of company interests, creating doubts as to whether the accountability gap has really been closed. In order to improve the public acceptance of standards and the credibility of monitoring, companies are increasingly willing to collaborate with other actors, notably with NGOs and in some cases with intergovernmental organizations (IGOs) and government agencies. In many areas, self-regulation is giving way to co-regulation, as NGOs, IGOs and government agencies are willing to take a role in the promotion and management of voluntary accountability schemes. It has been often the case that NGOs decided to support voluntary schemes after realizing that the prospects of mandatory social and environmental regulation at the international level were

63 Haufler, A Public Role for the Public Sector, op. cit., p. 33.

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poor. ‘As NGOs experienced repeated defeats in international arenas, they put more energy and resources into developing non-governmental programs.’ Many NGOs consider co-regulation a second best solution.

So-called ‘multi-stakeholder’ initiatives are often seen as an effective way to address the accountability gap of TNCs. Some proponents hail them as ‘third way’ between government regulation and corporate self-regulation. Some multi-stakeholder initiatives are limited to the standard-setting phase, while others include monitoring, certification and verification. A prominent example of the former type is the Global Reporting Initiative (GRI). The GRI, a collaborating centre of the UN Environment Programme, involves companies, corporations, NGOs, accountancy organizations, business associations and research institutes and aims to increase the credibility, consistency and comparability of corporate reporting on social and environmental issues. GRI creates process standards (Sustainability Reporting Guidelines) and keeps a record of the companies that have adopted them, but is not involved in monitoring or verifying compliance. The multi-stakeholder organization Social Accountability International (SAI) focuses on working conditions and performs a broader range of functions: it develops and updates the SA8000 performance standard based on ILO conventions, it trains and accredits independent auditors, it verifies public reports, and it publicizes a list of SA8000 certified facilities. The Fair Labor Association involves leading US apparel companies, universities and NGOs and its tasks include the development of an industry code of conduct, the accreditation of independent monitors, the facilitation of remediation in cases of non-compliance and the publication of instances of non-compliance and remediation. Other initiatives in which civil society organizations participate actively in the design and implementation of codes and standards are the Forest Stewardship Council, the Marine Stewardship Council, the Ethical Trading

66 See also the articles by Thorsten Brenner, Wolfgang Reinicke and Jan Martin Witte and by Thomas Risse in this issue.
Initiative and the Global Alliance for Workers and Communities. UN agencies participate in a number of them. In those initiatives, especially when they are initiated by NGOs, civil society organizations function as ‘accountability entrepreneurs’, bent on exploring new ways to improve the social and environmental performance and public accountability of business in light of the inadequacy of state action.

The Global Compact proposed by UN Secretary-General Kofi Annan is a prominent multi-stakeholder initiative that gained much attention since it was launched in 2000. It cannot be described as an accountability mechanism, however, as its aim is to generate ‘shared understandings’ about how companies can help promoting UN principles within corporate domains. The architect of the Global Compact, John Ruggie, describes it as a ‘social learning network’. It does not contemplate the possibility of sanctions for companies or verification of their statements. As the reputational risk associated with unfulfilled commitments within the Global Compact framework increases, however, the initiative might evolve into a multi-stakeholder accountability system.

External standard-setting and certification has clear advantages over unilateral or sectoral measures in terms of improving the public accountability of companies. It limits the discretion of companies with regard to what they can and cannot do and makes it likelier that a broader range of interests and concerns are taken into account in the definition of standards. Furthermore, external certification pro-

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70 Ruggie, ‘Taking Embedded Liberalism Global’, op. cit., p. 113. On the possibility of persuasion and learning in international affairs see the article by Thomas Risse in this issue.

71 The then Secretary-General of the International Chamber of Commerce, Maria Livianos Cattaui, stated that ‘Business would look askance at any suggestion involving external assessment of corporate performance, whether by special interest groups or by U.N. agencies’, ‘Yes to Annan’s “Global Compact” If It Isn’t a License to Meddle’, International Herald Tribune, 26 July 2000, quoted by Bruno and Karliner, Earthsummit.biz, op. cit., p. 53.

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vides information about compliance that can be substantially more credible and reliable than self-certification, especially if it involves key stakeholder groups. However, the capacity of multi-stakeholder initiatives to ensure accountability has limits. First, independent auditing may be performed in an inadequate way.72 Second, the very pluralisms of many multi-stakeholder initiatives can lead to damaging conflicts between different intermediaries in accountability relationships, for instance between NGOs and trade unions. Third, multi-stakeholder initiatives frequently have a narrow sectoral focus and have not expanded (yet) into domains where they would be particularly required.73 Fourth, many companies choose not to participate in partnerships, sometimes reaping free-rider benefits from the initiatives.74 This problem is exacerbated by the fact that the participating companies may not be those for which regulation would be most necessary,75 and that ‘lower profile competitor firms may largely avoid the cost of both compliance and public criticism’.76 The non-universal participation in voluntary schemes is their most serious shortcoming together with a fifth problem: the lack of enforcement mechanisms other than negative publicity for non-compliant companies. This problem, of course, is common to all voluntary approaches to corporate responsibility.77 Negative publicity may work as an instrument of accountability,78 but it suffers from the fact that

73 Utting, ‘Regulating Business’, op. cit., p. 82.
75 Hansen, ‘Environmental Regulation of Transnational Corporations’, op. cit., p. 177; interview, Anti-Slavery International.
76 Kline, ‘Business Codes and Conduct’, op. cit., p. 42.
77 It should be noted, however, that US courts are examining cases in which companies are accused by consumers of misrepresenting working conditions in their supply chains in promotional material.
78 Especially since the internet has intensified what Debora Spar calls the ‘spotlight’ phenomenon. Spar, ‘Foreign Investment and Human Rights’, op. cit.
the people who are able to punish companies (e.g. consumers in rich countries) are frequently not the same people whose interests the codes are supposed to protect (e.g., workers and communities in developing countries). This absence of congruence in the accountability relationship\(^79\) may lead to the underprovision of sanctions or to the use of sanctions that may be counterproductive (e.g., consumer boycotts). In addition, even if a substantial proportion of consumers and investors were willing to hold companies accountable for their behaviour abroad, they face serious collective action problems when it comes to applying sanctions.

If sanctioning is a problem for voluntary accountability mechanisms, it would be wrong to assume that sanctions are all that matter in inducing companies to improve their social and environmental performance. Research in global standard-setting has stressed the importance of ‘webs of dialogue’ in ensuring compliance with existing standards as well as promoting their ‘continuous improvement’.\(^80\) ‘Globalized rules and principles can be of consequence even if utterly detached from enforcement mechanisms.’\(^81\) To institutionalize such a web of policy dialogue and to promote the ‘global public domain’ is clearly the intention of the architects of the Global Compact. However, in these cases the progress and ‘ratcheting-up’ of business self-regulation does not necessarily occur as a result of the operation of accountability mechanisms.

CONCLUSION

The globalization of production exacerbates accountability gaps in the relationship between citizens and corporations. Some of these gaps stem from the difficulties that governments have in holding TNCs accountable under conditions of sustained capital mobility and opportunities for jurisdictional ‘exit’. Other gaps stem from the difficulties that citizens have in holding their government accountable when it colludes with, and receives support from, economically robust corporations – and TNCs tend to be robust in comparison to

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\(^79\) Held, Democracy and the Global Order, op. cit.

\(^80\) Braithwaite and Drahos, Global Business Regulation, op. cit., p. 615. On the role of persuasion and learning in transnational relations see the article by Thomas Risse in this issue.

\(^81\) Ibid., p. 10.

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many host countries. Finally, sometimes governments are too weak to function as effective links in the accountability chain between citizens and companies. All these accountability gaps are particularly worrying in developing countries.

On the whole, the problem might not be as severe as asserted by some anti-corporate activists. Most governments still possess impressive resources that can be used in their interactions with corporations, most of all their control over access to territory. Furthermore, the trend towards the democratization of national political systems enhances the influence of ordinary citizens on social and economic policies, including those affecting the operations of TNCs. Notwithstanding these countervailing trends, the power of large corporations is rightly perceived as a reason for concern by many citizens and political groups in the developing and the developed world. On balance, FDI may be beneficial to home and host countries, but the risk of socially and environmentally irresponsible behaviour by companies (especially in extractive industries) warrants concerted efforts to close the gaps in public accountability.

Currently, voluntary mechanisms for corporate accountability are in greater favour than mandatory mechanisms, especially among business representatives (not surprisingly) but also among many representatives of civil society, who see multi-stakeholder initiatives and certification institutions as a promising way to steer business behaviour towards greater social and environmental responsibility. However, ‘certification remains a blunt and imperfect tool for augmenting the accountability of global firms’.82 Several NGOs turned to these institutions after experiencing disappointment with intergovernmental forums. It may well be possible that dissatisfaction with voluntary initiatives will boost demands for a binding international legal framework that is agreed on and enforced by states. A renewed emphasis on mandatory mechanisms is evident in the current dispute about the norms on TNC responsibilities that have been adopted by a UN panel of independent experts in August 2003.83

82 Gereffi et al., ‘The NGO-Industrial Complex’, op. cit.
These norms bring together a range of obligations drawn from existing international human rights, labour and environmental conventions, and are widely regarded as a first step towards binding regulation and monitoring of TNC activities by UN bodies, backed by national enforcement. Leading human rights NGOs have celebrated the norms, whereas the main global business organizations – notably the International Chamber of Commerce and the International Organization of Employers – have condemned them for embodying a ‘legalistic’ approach to corporate responsibility. The norms will be debated by government representatives in the UN Commission on Human Rights in March 2004, and a fierce battle between business associations and NGOs can be expected.

This and other ongoing controversies suggest that, ultimately, the establishment of effective mechanisms for holding TNCs accountable may depend on the success of large-scale reforms of international institutions and the redefinition of their mandate. ‘Robust’ accountability mechanisms require state action, but this action is likely to remain problematic if international governance is not democratized. Where executive multilateralism has failed, societally-backed multilateralism may succeed.84

84 See the articles by Michael Zürn and David Held in this issue.