



## **Private Governance and the Potential of Private Law**

Hansen, Ole; Petersen, Clement Salung; Ulfbeck, Vibe Garf

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## Private Governance and the Potential of Private Law

Ole HANSEN\*, Clement Salung PETERSEN\* & Vibe ULFBECK\*

**Abstract:** *Private governance* can be defined as the phenomenon of private actors pursuing public goals and interests in the exercising of traditional state functions in the forms of rulemaking, implementation and dispute resolution. Private governance in these three ‘columns’ can have different sources and can be either ‘state driven’ or ‘market driven’. Whereas implications of private governance have to some extent been explored in public law, this article analyses the legal implications in private law and suggests a specific systematic approach. As examples, we focus on the supply chain as a market driven private governance system and the private provision of universal services as a state driven private governance system. The analysis shows how such private governance systems pose an immense challenge to the existing doctrines of private law and create considerable legal uncertainty. The analysis also leads to two more precise findings: (1) a private law analysis can benefit from focusing on the interplay between private governance in the three columns, and (2) the implications in private law seem to be of a different nature in the market driven as compared to the state driven private governance systems analysed.

**Résumé:** La gouvernance privée peut être définie comme le phénomène par lequel des acteurs privés poursuivent des objectifs publics dans l’exercice de fonctions traditionnellement étatiques telles que la réglementation, l’exécution et la résolution des litiges. La gouvernance privée peut dans le contexte de ces trois ‘piliers’ avoir des sources différentes et émaner soit de l’état soit du marché. Bien que les implications de la gouvernance privée ont dans une certaine mesure fait l’objet de recherches en droit public, le présent article en analyse les implications juridiques en droit privé et propose une approche systématique spécifique. Concrètement, nous nous focalisons sur la chaîne logistique comme un exemple de gouvernance privée menée par le marché et sur la fourniture par des acteurs privés de services universels comme un exemple de gouvernance privée émanant de l’état. Notre analyse montre comment de tels systèmes de gouvernance privée représentent un défi considérable pour les doctrines de droit privé existantes et peuvent créer une incertitude juridique importante. Notre analyse mène également à deux conclusions plus précises: 1) une analyse de droit privé peut bénéficier d’une concentration sur l’interaction entre les éléments de gouvernance privée à travers les trois piliers, et 2) les implications pour le droit privé semblent dans les systèmes analysés être de différente nature suivant si on

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\* The authors are Professors at Law at the Faculty of Law, University of Copenhagen, Centre for Private Governance (CEPRI), Denmark. We wish to thank Postdoc Carola Glinski, Associate Professor Silvia Adamo and Associate Professor Sylvie Cavaleri for help and valuable comments during the preparation of this article. We wish to thank student assistant Mille Skjold for editorial assistance. We are also thankful to Professor Bent-Ole Gram Mortensen for fruitful discussions on energy law. The final version of this article was submitted on 5 September 2019. Emails: ole.hansen@jur.ku.dk, clement.petersen@jur.ku.dk & vibe.ulfbeck@jur.ku.dk.

se concentre sur la gouvernance privée émanant du marché ou sur celle qui est conduite par l'état.

**Zusammenfassung:** Private Governance kann definiert werden als das Phänomen, dass private Akteure Gemeinwohlziele und öffentliche Interessen verfolgen und dabei Funktionen in Form der Schaffung, der Umsetzung und der Durchsetzung von Regeln ausüben, die traditionell dem Staat zugeschrieben werden. Private Governance in diesen drei Säulen kann unterschiedliche Ursachen haben und entweder durch den Staat oder durch den Markt initiiert werden. Während die Implikationen von Private Governance für das Öffentliche Recht zu einem gewissen Teil bereits untersucht wurden, analysiert dieser Beitrag die rechtlichen Auswirkungen auf das Privatrecht und verfolgt dabei einen spezifischen systematischen Ansatz. Als Beispiele wählen die Autoren Lieferketten als privat-initiierte Governancesysteme und die private Erbringung von Universaldienstleistungen als staatlich-initiierte Governancesysteme. Die Analyse zeigt, dass solche Governancesysteme eine große Herausforderung für die traditionelle Privatrechtslehre darstellen und erhebliche Rechtsunsicherheit mit sich bringen. Darüberhinaus kommt sie zu zwei präziseren Ergebnissen: (1) Die privatrechtliche Analyse profitiert von der Fokussierung auf das Zusammenspiel von Private Governance in den drei genannten Säulen. (2) Die Implikationen für das Privatrecht unterscheiden sich je nachdem, ob das Governancesystem staatlich oder durch den Markt initiiert ist.

## 1. Introduction

### 1.1. *The Concept of Private Governance, Its Levels and Sources*

This article concerns the role of private law in different types of private governance systems. It starts out by defining the concept of private governance and by putting it into context.

Private actors have always had considerable room for regulating market activity. Through choice of organization and contractual practices, they may create their own legal orders by prescribing their own rules and standards of behaviour. They also play a significant role in the implementation of such private legal orders and finally, private actors may choose their own means of dispute resolution. In this way, the activities of private actors can be seen as mirroring all of the traditional state governance functions in the forms of rulemaking, implementation and dispute resolution. The term *private governance* may be used to describe such activities of private actors.

In recent decades, different societal developments seem to have expanded the room for private governance of both traditional commercial activities and the supply of a variety of goods and services of critical importance to markets and welfare. Budgetary constraints and general ideological and political movements have led many welfare states to liberalization of markets and *privatization* of what they previously considered 'public tasks', including the provision of services of general interest and (other) welfare services.<sup>1</sup> Supported by *globalization* and *digitalization*, an increasing number of private actors operate as powerful entities

on transnational (sometimes even global) markets challenging the governing role and reach of states. The societal impact of some private actors has created a public call for private actors to safeguard certain public values and interests in their private governance. For example, we have witnessed an increasing interest amongst private actors in voluntarily pursuing public values and interests such as human rights, social policy, health and environmental protection through private standard setting and/or Corporate Social Responsibility policies (CSR). With these developments, private governance has become a matter of general public interest.

Thus, terminologically, one could speak of *public interest private governance* or *public private governance* covering the types of situations just mentioned. In contrast, the term *private interest private governance* or *private private governance* can be used for describing situations in which private governance is a tool for regulating purely commercial activities that do not seek to pursue values and goals in the public interest. As an example could be mentioned commercial contracts that define the duties of the parties to the contract (regulation), stipulate the way in which the contract is to be carried out (implementation) and the way in which disputes are to be solved (dispute regulation). *Private private governance* has been widely dealt with in such classical disciplines as contract law, company law and (international) commercial arbitration.<sup>2</sup> *Public private governance*, in contrast, does not fall within any of the classical legal categories. In this article, we use the term *private governance* as shorthand for *public private governance*.<sup>3</sup>

Private governance occurs both at the *domestic level*, the *regional level* and the *transnational level*. For example, much privatization takes place at the local level, either through asset privatization or contracting out of public services from the

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- 1 See e.g. the examples mentioned in section 3.3 *infra*. We are aware that there are considerable differences between the socioeconomic models of different states (what in one state has traditionally been 'public' may in other states have been 'private'). Thus, the division between a private and a public sector varies considerably from one national economy to another, depending on e.g. historical positions, stage of development and recent political strategies.
  - 2 The term *private governance* is sometimes used in this way, i.e. as more or less equal to *contract law matters* or discussions on the extent to which there is or should be *freedom of contract* in a certain area.
  - 3 It is important to be aware that the different social sciences do not use the term *governance* in a coherent way, see Kess VAN KERSBERGEN & Frans van WAARDEN, "'Governance' as a bridge between disciplines: Cross-disciplinary inspiration regarding shifts in governance and problems of governability, accountability and legitimacy", 43. *EJPR (European Journal of Political Research)* 2004, pp 143-171.
  - 4 It could be argued that private governance appears in a special version at the EU level where EU law through the fundamental freedoms both shapes and drives the contours of the phenomenon, Fritz W. SCHARPF, 'The asymmetry of European Integration, or why the EU cannot be a social market economy', 8. *SER (Socio-Economic Review)* 2010, pp 211-250. Such 'EU Private Governance' is not specifically addressed in this article.

public sector to private actors. However, privatization also occurs at the regional level for example at the EU level through liberalization of markets.<sup>4</sup> Finally, privatization takes place at the transnational level for example in the shape of international product and/or technical standards created by private actors determining quality and safety requirements and thereby market entry requirements.<sup>5</sup>

The examples above show that private governance has different sources. Two different bases for private governance can be distinguished. In the first situation, private actors voluntarily undertake ‘public tasks’ or seek to safeguard public values and interests without any legal obligation to do so under applicable state laws, and the legal basis of such private governance is then inherently private and ‘market driven’. The voluntary pursuance of CSR goals by private companies can be seen as an example of market driven private governance. In the second situation, the state has ‘delegated’ governance power to private actors on the condition that the private actors safeguard certain public values and interests, and in this sense the source of such private governance becomes public or *state driven*. The outsourcing of the performance of universal services to private actors from the state is an example of state driven private governance. Several intermediate positions exist.<sup>6</sup> In this way, private governance arises within different normative structures.<sup>7</sup>

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- 5 As examples could be mentioned the ISO standards defining technical requirements for different products, the SAI standards applicable in social audits, environmental standards developed by the Forest Stewardship Council and the Marime Stewardship Council and product standards developed by CEN and CENELEC. On food safety standards as governance mechanisms, see J. WOULTERS, A. MARX & N. HACHEZ, *Private Standards, Global Governance and Transatlantic Cooperation – The Case of Global Food Safety Governance* (Leuven: Centre for Global Governance Studies), pp 1–30; T.D. LYTTON, ‘Exposing private third-party food safety auditors to civil liability for negligence: Harnessing private law norms to regulate private governance’, 27. *ERPL (European Review of Private Law)* 2019, pp 353–370. On private standards and the role of tort law in general, see P. VERBRUGGEN, ‘Good Governance of Private Standardization and the Role of Tort Law’, 27. *ERPL (European Review of Private Law)* 2019, pp 319–352.
- 6 As noted by P. VERBRUGGEN, ‘Introduction: Regulating Private Regulators: Understanding the Role of Private Law’, 27. *ERPL (European Review of Private Law)* 2019, p (175) at 178: ‘Even though private regulation is primarily driven by private actors, links with the state or state regulation are abundant’ and p 1979: ‘... private regulation is frequently the outcome of an iterative process of interaction between public and private actors both at national and international level’.
- 7 The basic distinction between market driven and state driven private governance is also found in E. BENEVENISTI & G.W. DOWNS, ‘National courts and transnational private regulation’, in F. Cafaggi (ed.), *Enforcement of Transnational Regulation* (Edward Elgar Publishing 2012), p 131: ‘Such private initiatives result from full or partial delegation of authority by governments to private actors or from new private initiatives that are approved, tolerated, or left unnoticed by overburdened governments’. See also R. BROWNSWORD, R.A.J. VAN GESTEL & H-W. MICKLITZ, ‘Introduction – Contract and regulation: Changing paradigms’, in R. Brownsword, R.A.J. van Gestel & H-W. Micklitz (eds), *Contract and Regulation. A handbook on new methods of lawmaking in private law* (Edward Elgar Publishing 2017), p 10, distinguishing between on the one hand ‘(state initiated) contract law and on the other self-regulation (by commercial contractors and merchants)’.

Both the different levels and different sources of private governance may have legal implications (see further below).

### **1.2. *Private Governance in Context and Legal Research Questions in Private Governance***

Since the concept of private governance builds on the classical distinction between state and market it is also related to the distinction between private law and public law. Traditionally, public law has been described as concerned with the legal position of public entities *vis-à-vis* other public entities or private actors, whereas private law is concerned with the legal relationship between private actors. Public activity must generally have a (statutory) legal basis, whereas private actors have party autonomy unless limited by law. Today, it is widely accepted that the distinction between public law and private law is blurred and that for instance statutory regulation of certain relations between private parties (e.g. in the area of consumer law) can be labelled 'private law'.<sup>8</sup> Despite this reservation as to the clarity of the distinction, public and private law are rooted in inherently different and mutually conflicting principles and values. While public law is based on principles of e.g. legality, authority and objectivity (non-discrimination), private law deduces its legitimacy from principles of autonomy, consent and mutuality.<sup>9</sup> Private governance challenges the distinction between private law and public law by suggesting the use of private actors in the pursuance of public tasks and in the safeguarding of public values and interests. For this very reason, the distinction between public law and private law also represents the fundamental analytical tool for an examination of the legal implications of private governance.

Against this background, the phenomenon of private governance can be seen as giving rise to both public law and private law questions.<sup>10</sup> Whereas the legal

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8 For one of the more recent works on this, see L. VAN DEN BERGE, 'Rethinking the Public-Private Law Divide in the Age of Governmentality and Network Governance', 5. *EJCL (European Journal of Comparative Law and Governance)* 2018, pp 119-143, with further references.

9 It has been argued that there are no fundamental differences between values in public and private law, see e.g. CAROLA GLINSKI, *Die rechtliche Bedeutung der privaten Regulierung globaler Produktionsstandards* (Nomos 2011), pp 89 ff, pp 266 ff and pp 285 ff.

10 Public law may both support and limit private governance. Examples of a limiting effect may be found in competition law, see G. MONTI & J. MULDER, 'Escaping the Clutches of EU Competition Law. Pathway to assess private sustainability Initiatives', 42. *ELR (European law review)* 2017. With regard to global private governance, an example is regulation which in accordance with public international law has extraterritorial effect. Also mentioned could be international investment treaties between states that on one hand provide the private actor with a private dispute resolution mechanism but at the same time may interfere with the role of contract as a regulatory tool between the state and the investor. It has been argued that also trade law in the circumstances may pose challenges to private CSR regulation, for an analysis see C. GLINSKI, 'CSR and the Law of the WTO - The Impact of Tuna Dolphin II and EC-Seal Products', 1. *NJCL (Nordic Journal of*

implications of private governance in public law have been rather intensely studied,<sup>11</sup> often within the discourses of new governance<sup>12</sup> and global governance,<sup>13</sup> which

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*Commercial Law*) 2017, pp 121. See also M. MATAJKA, 'Leveraging Trade Law for Governance Reform: The Impact of the WTO Agreement on Technical Barriers to Trade on Private Standard Setting' 27. *ERPL (European Review of Private Law)* 2019, pp 293-318. Public procurement law can have both a limiting and a supporting effect on private governance, see e.g. M. ANDRECKA (guest ed.), 'Procurement beyond price: Sustainability and CSR in public purchasing', 3. *The Special Issue EPPPL (European Procurement & Public Private Partnership Law Review)* 2017. With regard to private law questions in private governance, see further below.

- 11 See for instance Gillian E. METZGER, 'Privatization as delegation', 103. *CLR (Columbia Law Review)* 2003, p 1367; J. FREEMANN, 'The private role in public governance', 75. *NYULR (NYU Law Review)* 2000, p 543; H. SCHEPEL, *The Constitution of Private Governance: Product Standards in the Regulation of Integrating Markets* (Hart Publishing 2005); M. MINOW, *Partners Not Rivals: Privatization and the Public Good* (Beacon Press 2003). Micklitz notes with regard to privatization in the telecommunications, energy and transport sector that the overwhelming amount of literature has focused on the public law side, i.e on the concept, the regulatory devices, etc., see H-W. MICKLITZ, *The invisible hand* (Working paper), p 16. Also P. VERBRUGGEN, 27. *ERPL* 2019, p (175) at 180 observes that private regulatory activities have mainly been dealt with from a public law angle.
- 12 New governance scholarship developed in the 1990s and focuses - broadly speaking - on the move from 'control and demand' modes of governance to more flexible structures involving both private actors and civil society at the domestic level. Legal new governance scholarship is often at a fairly abstract level and often as partly interdisciplinary research, often focusing on the challenges to democracy brought about by new governance models, see e.g. O. LOBEL, 'New Governance as regulatory governance', in D. Levi-Faur (ed.), *The Oxford Handbook of Governance* (Oxford University Press 2012), focusing on the reasons for the development and the benefits of it; E. KORKEA-AHO, 'What is new about new governance', 32. *Retfærd* 2009(1), focusing on law and policy issues including the challenges to democracy posed by new governance models; M.P. VANDENBERGH, 'Environmental Private Governance', 99. *CLR (Cornell Law Review)* 2013, p 129, focusing on the potential of private actors filling the gap left by lack of governmental governance; V. JONES, *The New Public Contracting - Regulation, Responsiveness, Relationality* (Oxford: Oxford University Press 2006), analysing the use of contract as a regulatory mechanism in government policies, applying a socio-legal inter-disciplinary perspective.
- 13 Global Governance scholarship is concerned with parallel phenomena at the global level. It includes studies of International Governmental Organizations (IGOs), Public-Private Partnerships, Private Governance and Tripartite governance. For more recent overviews, see for instance J. JANG, J. MCSPARREN & Y. RASHCHUPKINA, 'Global governance: Present and future', 2. *Palgrave Communications* 2016, giving a political science perspective on the theme of shifting relations of power, embedded in global governance. See also F. BIERMANN & P. PATTBURG, 'Global Environmental Governance: Taking Stock, Moving Forward', 33. *Annual Review of Environment and Resources* 2008, pp 277-294, describing how world politics on environmental law are no longer confined to the governments of nation states; E.P. STRINGHAM, *Private Governance* (Oxford: Oxford University Press 2015), looking at private governance in the financial sector from an economic angle and arguing that government enforcement is not necessary for the development of advanced markets. Legal global governance scholarship include the founding work K.W. ABBOTT & D. SNIDEL 'Strengthening International Regulation Through Transnational New Governance: Overcoming the orchestration Deficit', 42. *VJTL (Vanderbilt Journal of Transnational Law)* 2009, pp 501-578, introducing the perspective of new governance models at the global level and combing

both include private governance as an element, until recently, the implications of private governance in private law had hardly been addressed in legal research. Only within the last 5–10 years has the topic started to surface as a research area. Some of the first private law contributions have been at the more abstract level.<sup>14</sup> At the European level until 2008, the debate about European private law mainly focused on the question of harmonization of rules through common codes.<sup>15</sup> However, around this time a new discourse was introduced. It focuses on what has been termed ‘regulatory private law’ and basically has two strings. One focuses on market driven phenomena.<sup>16</sup> The other one takes its starting point in state driven phenomena.<sup>17</sup>

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a political science angle with a legal angle. Part of the literature is concerned with the ‘fragmentation’ and ‘stagnation’ of international law, see F. BIERMANN, P. PATTEBERG, H. VAN ASSELT & F. ZELLI, ‘The fragmentation of Global Governance Architectures: A Framework for Analysis’, 9. *Global Environmental Politics* 2009, pp 14–40; M. KOSKENNIEMI & P. LEINO ‘Fragmentation of International Law? Post modern Anxieties’, 15. *LJIL (Leiden Journal of International Law)* 2002, pp 553–579; J. PAUWELYN, R.A. WESSEL & J. WOUTERS, *When Structures become Schakles: The Stagnation of International Law* (Leuven: Leuven Centre for Global Governance Studies 2012), Working paper no. 97.

- 14 As an example can be mentioned G. CALLIESS & P. ZUMBANSEN, *Rough Consensus and Running Code: A Theory of Transnational Private Law* (Hart Publishing 2012), which focuses on areas such as consumer law and company law with a view to ‘illuminating the processes by which regulatory structures [in these areas] are emerging’ and ‘how they are conceptualised from a political science, a legal and an economic perspective’ (p 23); L.C. BACKER, *On the Tension between Public and Private Governance in the Legal Order: State Ideology and Corporation in Polycentric Asymmetric Orders* (Consortium for Peace and Ethics 2012), questioning ‘state ideology’ as a concept for analysing transnational governance phenomena.
- 15 See review by J. SMITH of F. CAFFAGGI & H. MUIR-WATT, ‘Making European Private Law’, 28. *Yearbook of European Law* 2009, pp 705–709, doi.org/10.1093/yel/28.1.705.
- 16 See F. CAFFAGGI & H. MUIR-WATT (eds), *Making European Private Law: Governance Design* (Edward Elgar Publishing 2008), focusing on whether and how European private law can be brought about by other means than as a common code. It points *inter alia* to private regulation and discusses legitimacy problems. See also F. CAFFAGGI & H. MUIR-WATT (eds), *The Regulatory Function of European Private Law* (Edward Elgar Publishing 2009), discussing whether and how European private law can pursue regulatory functions beyond market integration, and F. CAFFAGGI, *Enforcement of Transnational Regulation: Ensuring Compliance in a Global World* (Edward Elgar Publishing 2012), the purpose of which is to map enforcement mechanisms.
- 17 See H-W. MICKLITZ, ‘The Visible Hand of European Private Law’, in P. Eckhout & T. Tridimas (eds), 28. *Yearbook of European Law 2009* (Oxford: Oxford University Press 2010), pp 3–60; H-W. MICKLITZ, ‘Nation State Private Laws and European Regulatory Private Law’, in E. Arcelia & Q. Adriano (eds), *The Evolution of Global Trade over the Last Thirty Years*, (Universidad Nacional Autónoma de México 2013), pp 251–274; H-W. MICKLITZ & Y. SVETIEV, ‘The Transformation of Private Law’, in H-W. Micklitz, Y. Svetiev & G. Comparato (eds), *European Regulatory Private Law – The Paradigm Tested* (EUI-ERC Law 2014/04), pp 69–97; H-W. MICKLITZ, ‘The Transformation of Enforcement in EU Private Law: Preliminary Considerations’ 23. *ERPL (European Review of Private Law)* 2015, pp 491–524; R. BROWNSWORD, R.A.J. VAN GESTEL & H-W. MICKLITZ, *Contract and Regulation: A Handbook on New Methods of Law Making in Private Law* (Edward Elgar Publishing 2017). An early example of thoughts on regulatory private law is H.

Only very recently, the need for (more) private law work in this field was clearly expressed in a special issue in this Law Journal consisting of a series of articles undertaking concrete private law analysis of the phenomenon of private regulation.<sup>18</sup>

### 1.3. *Aim and Conceptual Framework*

In this article, we attempt to establish a conceptual framework for a systematic analysis of the legal implications of private governance in private law. We focus on the extent to which private law is able to serve as a tool for fulfilling public tasks and protecting public values and interests in private governance systems, i.e. to what extent private law has ‘governance potential’. We focus in particular on contract law and tort law as two fundamental building blocks in private law.

Based on the observations above, our conceptual framework has two dimensions. On the one hand, we distinguish between the three governance functions of regulation (rulemaking), implementation (including control, supervision and other types of administration as well as the provision of ‘public’ services) and dispute resolution. On the other hand, we distinguish between the two different bases for private governance, namely the market and the state. Based on these distinctions we analyse two examples of private governance: The first is private governance in global supply chains, which represents an example of transnational, market driven private governance. The second is private governance in the provision of universal services, which represents an example of domestic, state driven private governance.<sup>19</sup> Both examples illustrate governance systems which involve several private actors.<sup>20</sup> Below is a graphical overview of our conceptual framework and the

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COLLINS, *Regulating contracts* (Oxford: Oxford University Press 1999). In American legal literature the term ‘publization’ has been introduced to describe how privatization may be used as a tool to implement public values and interest into private markets, cf. in particular J. FREEMAN, ‘Extending Public Norms through Privatization’, 116. *HLR (Harvard Law Review)* 2003(5), pp 1285-1352. See also J. FREEMAN, ‘The Contracting State’, 28. *FLA. ST.U.L.REV (Florida State University Law Review)* 2000, pp 155-214. In line with this author, others have anticipated that administrative law may be used as a tool for controlling market activity, see e.g. A.C. AMAN JR., ‘Privatization and Democracy: Resources in Administrative Law’, in J. Freeman & M. Minow (eds), *Government by Contract* (Cambridge, Massachusetts: Harvard University Press 2009); A.C. AMAN JR., ‘Administrative Law for a New Century’, in Michael Taggart (ed.), *The Province of Administrative Law* (Oxford: Hart Publishing 1997), pp 90-117.

18 P. VERBRUGGEN (ed.), ‘Regulating Private Regulators: Understanding the Role of Private Law, special issue 2019’. *ERPL (European Review of Private law)* 2019, focusing on the ‘regulatory’ dimension of private law with regard to private regulators.

19 In the chosen example, the domestic statutory law is based on EU law. In this sense, the case also represents an example of state driven private governance at the EU level.

20 Other private governance systems may involve only one actor, fulfilling all three governance functions. As an example could be mentioned digital platforms, see C. PETERSEN, V. ULFBECK & O. HANSEN, ‘Platforms as Private Governance Systems - The Example of Airbnb’ 1. *NJCL (Nordic Journal of Commercial Law)* 2018, pp 39 et seq.

specific aspects of private governance that we will analyse in part 2 and 3 of this article.

<i>Governance Function</i>	<i>Regulation</i>	<i>Implementation</i>	<i>Dispute Resolution</i>
<i>Source</i>			
Market driven - The example of global supply chains	CSR obligations	Social auditing	Mediation
State driven - The example of the provision of universal services	State regulation and contracts	Private providers of universal services	Arbitration

More specifically, we will use this conceptual framework to make a systematic examination of (1) the implications for private law analysis of the possible interplay between the different private actor functions in the governance system (cross column analysis) and (2) the extent to which private law is challenged when serving as a tool for the protection of public interests and values, and whether the challenges are of the same or a different nature in market driven and state driven governance systems.

## **2. Private Governance Emerging from the Market: The Example of Global Supply Chains**

### **2.1. Introduction**

Globalization has led to a fragmentation of production. Thus, today different parts of the production are outsourced from powerful companies, often based in the Global North, to suppliers often based in the Global South. The suppliers can be either subsidiaries of the parent company or purely contracted companies. This outsourcing, whether based on ownership or contract or a mixture of these, creates multi-tiered chains of companies, often referred to as supply chains or global value chains. Supply chains may be structured in different ways but many of them have in common that the buyer company to some extent controls the chain by choosing suppliers and by setting - directly or indirectly - the terms of the contracts in the chain. For this reason, the buyer is sometimes called the 'chain leader' or the 'lead company'. The supply chain in many ways functions as a whole and raises questions of both regulation, implementation and dispute resolution, often at the transnational level.

Since supply chains function as dominant players in the market, the question of the responsibility of the companies in the chain to pursue social goals (CSR) or, more

broadly, ‘sustainability goals’ has attracted much attention<sup>21</sup> and it has become common for companies to take on CSR responsibilities. In this sense, although CSR initiatives are to some extent encouraged by state initiatives both at the national and the international level and there seems to be a general expectation in society that companies do pursue CSR goals, CSR commitments are voluntarily undertaken by the companies and can be seen as signifying a market driven movement.<sup>22</sup>

In the following, we undertake a private law analysis of this phenomenon. We identify challenges to private law when used as a tool for pursuing public interest and values in the governance system and we show that a private law analysis will often require looking at different functions in the governance system in combination (cross column analysis).

## 2.2. Regulation: CSR Obligations

In pursuing CSR goals and making visible their commitments, chain leaders may choose to sign up for an existing private CSR standard such as for example the SA 8000 standard developed by the NGO Social Accountability International (SAI),<sup>23</sup>

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- 21 At the international level, initiatives include the UN Global Compact, see [unglobalcompact.org](http://unglobalcompact.org), and the UN Guiding Principles on Business and Human Rights, see J. RUGGIE, in UN Document *Guiding Principles on Business and Human Rights: Implementing the United Nations ‘Protect, Respect and Remedy’ Framework* (2011), [ohchr.org/documents/publications/Guiding\\_principlesBusinesshr\\_eN.pdf](http://ohchr.org/documents/publications/Guiding_principlesBusinesshr_eN.pdf); UN Document *Report of the Special Representative of the Secretary General on the issue of human rights and transnational corporations and other business enterprises* (31 March 2011), A/HRC/17/31, [ohchr.org/documents/issues/business/A.HRC.17.31.pdf](http://ohchr.org/documents/issues/business/A.HRC.17.31.pdf); the OECD Guidelines, see *OECD Guidelines for Multinational Enterprises of 2011*, [oecd.org/mne/48004323.pdf](http://oecd.org/mne/48004323.pdf). At the EU level, non-financial reporting requirements have been introduced, see Dir. 2014/95 of 22 October 2014 amending Dir. 2013/34/EU as regards disclosure of non-financial and diversity information by certain large undertakings and groups, [data.europa.eu/eli/dir/2014/95/oj](http://data.europa.eu/eli/dir/2014/95/oj).
- 22 In two European jurisdictions, France and Switzerland, governments have taken initiatives to compel companies to the pursuance of CSR goals. The French initiative makes it compulsory for companies to adopt a vigilance plan concerning activities of the company and the activities of the subsidiaries or companies it controls, see Loi no. 2017-399 du 27 mars 2017 relative au devoir de vigilance des sociétés mères et entreprise donneuses d’ordre (France), [www.legifrance.gouv.fr/eli/loi/2017/3/27/2017-399/jo/texte](http://www.legifrance.gouv.fr/eli/loi/2017/3/27/2017-399/jo/texte). For information on the Swiss proposal, see [corporatejustice.ch/](http://corporatejustice.ch/). States may also pursue sustainability and CSR goals through public procurement, see *inter alia*, the special issue on this in M. ANDRECKA (ed.), 12. *European Procurement & Public Private Partnership Law Review* 2017.
- 23 See [sa-intl.org/index.cfm?fuseaction=Page.ViewPage&pageId=1842](http://sa-intl.org/index.cfm?fuseaction=Page.ViewPage&pageId=1842). Under this system, certification is mandatory. The certifiers are accredited by Social Accountabilty Accreditation Services (SAAS) which is an institution under the SAI. By signing up to the SA8000 system, the chain leader undertakes a contractual obligation towards SAI to subject to certification.

sign up for a system developed by a certification body,<sup>24</sup> enter into an agreement with NGOs,<sup>25</sup> sign up to a system like the Bangladesh accord system<sup>26</sup> or simply develop its own rules. Chain leaders often incorporate the chosen CSR principles into a code of conduct and require their business partners to observe this code.<sup>27</sup> In this way, a code of conduct may regulate the activities of the companies that are part of the chain. The codes of conduct can be seen as private ‘legislation’ in the sense that they pertain to apply to multiple parties and address issues of a public law nature concerning workers’ rights, human rights, environmental protection and anti-corruption measures.

The codes of conduct adopted by the chain leaders are often incorporated into the contracts with the suppliers.<sup>28</sup> Often the contract between the chain leader and the supplier will contain an obligation on the part of the supplier to comply with the code and also to ensure code compliance by the supplier’s supplier(s).<sup>29</sup> This development raises the question whether such clauses can be enforced through private law.

With regard to CSR clauses in supply chains, research shows that although CSR commitments are ‘dressed’ in contractual clothing, this type of clause cannot always be enforced in classical contract law.<sup>30</sup> Firstly, CSR obligations will not always be found in the contract itself but in appendices or on a website, and in order to make the argument that the clauses form part of the contract it may be

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- 24 T. VAN HO & C. TERWINDT, ‘Assessing the Duty of Care for Social auditors’, 27. *ERPL (European Review of Private Law)* 2019, pp 379, 283.
- 25 C. GLISNKY & P. ROTT, ‘The Role and Liability of Certification Organisations in Transnational Value Chains’ 23. *DLR (Deakin Law Review)* 2018, pp 83, 111.
- 26 J. SALMINEN, ‘The Accord on Fire and Building Safety in Bangladesh: A New Paradigm for Limiting Liability in Global Supply Chains?’, 66. *AJCL (The American Journal of Comparative Law)* (2), pp 411-451.
- 27 V. ULFBECK, O. HANSEN & A. ANDHOV, ‘Enforcement of CSR clauses by contract’, in V. Ulfbeck, A. Andhov & K. Mitkidis (eds), *Responsible Supply Chain Management* (Routledge 2019), p 47; K. MITKIDIS, ‘Enforcement of sustainability contractual clauses in supply chains by third parties’, in V. Ulfbeck, A. Andhov & K. Mitkidis (eds), *Responsible Supply Chain Management* (Routledge 2019), p 65.
- 28 V. ULFBECK, O. HANSEN & A. ANDHOV, in *Responsible Supply Chain Management*, p 47 with further references.
- 29 See for instance K. MITKIDIS, *Sustainability Clauses in International Business Contracts* (Eleven International Publishing 2015), p 201.
- 30 For general studies of this within different national legal systems and in international contract law, see A. BECKERS, *Enforcing Corporate Social Responsibility Codes: On Global Self-Regulation and National Private Law* (Hart Publishing 2015); K. MITKIDIS, *Sustainability Clauses in International Business Contracts*; A.L. VYTOPIL, *Contractual Control in the Supply Chain: On Corporate Social Responsibility, Codes of Conduct, Contracts and (Avoiding) Liability* (Eleven International Publishing 2015); A. RÜHMKORF, *Corporate Social Responsibility, Private Law and Global Supply Chains* (Elgar Publishing 2015); V. ULFBECK, O. HANSEN & A. ANDHOV, in *Responsible Supply Chain Management*.

necessary to rely on theories of incorporation by reference or implied terms.<sup>31</sup> Secondly, even if the CSR obligations are found in the contract they may be perceived of as non-legal, only ethical obligations and in addition, the CSR commitments may be formulated so vaguely that enforcement of the clauses will require relying on contract law theories which lower the bar for formation of contracts as compared to classical contract law.<sup>32</sup> Thirdly, it may be difficult to apply classical contractual remedies to CSR clauses. For instance, it may be difficult to calculate a compensatory claim for not living up to climate goals in the contract or for creating reputational damage on the part of the lead firm by ignoring CSR provisions.<sup>33</sup> More fundamentally, the basic evaluation of whether there is a breach of the contract at all may be complicated if the CSR obligations are formulated in imprecise and vague language. Apart from these challenges in applying classical contract law mechanisms, the parties to the contract may be less inclined to use these mechanisms at all. In reality, the buyer may be more interested in securing a long term relationship with the supplier by having an ongoing dialogue with the supplier as to how to live up to the CSR obligations. Again, classical contract law, based on the assumption that the contracting parties are adversaries, may be ill-equipped for dealing with this kind of relation, and handling CSR issues in the supply chain may call for the use of less traditional contractual instruments such as adjustments of the contract on the basis of fairness principles or renegotiation, i.e. tools that are more familiar to a relational contract law theory.<sup>34</sup>

Another reason why the buyer may have no real interest in securing the adherence to the CSR clauses is that they – given their public law nature – basically concern third party interests (and in some situations also the public interest).<sup>35</sup> Contract law was primarily designed for handling the relation between the contracting parties, not the relation with third parties (or the public at large). Consequently, the enforcement of CSR clauses will often generate a need to rely on the exceptions to the principle of privity of contract such as third party beneficiary law, agency law and other third party constructions.<sup>36</sup> In sum, the

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31 V. ULFBECK, O. HANSEN & A. ANDHOV, in *Responsible Supply Chain Management*, p 50 with further references.

32 V. ULFBECK, O. HANSEN & A. ANDHOV, in *Responsible Supply Chain Management*, p 52 with further references.

33 K. MITKIDIS, *Sustainability Clauses in International Business Contracts*, pp 227 et seq. discusses the extent to which non-pecuniary loss consisting in reputational damage can be compensated and the problems related to showing that reputational loss has led to an economic loss.

34 In legal literature it has been pointed out that CSR clauses in general make the contract ‘more relational’, for instance K. MITKIDIS, *Sustainability Clauses in International Business Contracts*, p 95.

35 K. MITKIDIS, *Sustainability Clauses in International Business Contracts*, p 95 observes that sustainability clauses ‘straddle the thin line between bilateral agreements and regulation’.

36 As an example could be mentioned the Walmart case, Court of Appeals for the Ninth Circuit 10 July 2009, *Doe I v. Wal-Mart Stores, Inc.*, 572 F.3d 677 (9th Cir.2009), where the plaintiffs, who

phenomenon of CSR in the supply chain can be seen as challenging contract law in the sense that enforcement of the clauses often requires reliance on exceptions to the general core principles of contract law rather than the general principles themselves.

Whereas contract law may have difficulties in protecting third party rights, *tort law* may protect such rights. Tort law – as an enforcer of societal norms – is also capable of internalizing certain public values and interests such as workplace security, human rights, and the environment in its protective scope. Thus, tort law has developed from being primarily a personal injury law in the twentieth century into a much broader discipline.<sup>37</sup> However, also in tort law, limits of the protective reach of the liability rules are continuously tested by courts. *Bruggemeier* puts it this way: ‘Tort law judges adjudicate the scope of the individual and business freedoms within society ... These judicial policies imply a reassessment of the scope of protection of traditional legal rights. Judges are redefining areas of autonomy ...’<sup>38</sup>

Today, there is an overlap between protected interests under CSR policies and protected interests under tort law.<sup>39</sup> However, the overlap may not be total and in addition, the use of outsourcing business models may challenge the capability of tort law to protect such values. Firstly, outsourcing creates *distance* between the tortfeasor and the victims which makes it difficult to establish vicarious liability as well as a duty of care towards the victims. Secondly, outsourcing may remove the scene of the damage causing activities to societies with *lower standards* for social and environmental protection, raising the question whether voluntarily adopted CSR standards can be enforced by tort law.

With regard to the problem of distance, third parties have in number of cases attempted to sue lead firms for violations of workers’ rights or harm done to the environment by subsidiaries or contractual partners placed in the Global South.<sup>40</sup> Establishing vicarious liability on the part of the lead company for acts

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were injured workers of the supplier, attempted to rely on third party beneficiary law in suing the lead company for damages. For literature trying out third party constructions in contract law, see A. L. VYTOPIL, *Contractual Control in the Supply Chain*, Chs 7 and 8; A. BECKERS, *Enforcing Corporate Social Responsibility Codes*, pp 126–145; K. MITKIDIS, in *Responsible Supply Chain Management*, p 65.

- 37 G. BRUGGEMEIER, *Common Principles of Tort Law – A Pre-Statement of Law* (British Institute of International and Comparative Law 2004), p 10.
- 38 G. BRUGGEMEIER, *Common Principles of Tort Law*, p 11.
- 39 Making this point with regard to personal injuries, see for instance C. VAN DAM, ‘Tort Law and Human Rights: Brothers in Arms. On the Role of Tort Law in the Area of Business and Human Rights’, 2. *JETL (Journal of European Tort Law)* 2011, p 221.
- 40 Some examples include: Supreme Court 10 April 2019, *Vedanta Resources Plc and another v. Lungowe & others* UKSC 20, [www.supremecourt.uk/cases/docs/uksc-2017-0185-judgment.pdf](http://www.supremecourt.uk/cases/docs/uksc-2017-0185-judgment.pdf); Court of Appeal 14 February 2018, *Okpabi and others v. Royal Dutch Shell and Shell Petroleum Development Company of Nigeria*, EWCA Civ 191; Ontario Court of Appeal 20 December 2018, *DAS v. George Washington Limited*, 2018 ONCA 1053; The US case, Superior Court of the State of

and omissions in the supply chain is extremely difficult since it runs counter to both the basic company law principle of separate entities and the tort law principle that there is no vicarious liability for independent contractors.<sup>41</sup> Moreover, establishing direct liability is also not straightforward. Under ordinary tort law, it is the general rule that negligent acts may lead to liability, whereas it is normally more difficult to establish liability for omissions.<sup>42</sup> However, supply chain liability cases often concern omissions (for instance to safeguard the suppliers' workers' rights). In such cases, succeeding with a claim against the leadfirm demands proof that the leadfirm was under a duty of care towards the injured workers.

Recent English case law indicates that it may be possible to establish such a duty of care *vis-à-vis* more distant third parties, in particular by relying on the concept of assumption of responsibility. The principle is by some seen as a special gapfiller between tortious and contractual liability.<sup>43</sup> An example of an application of this principle is the much discussed case *Chandler v. Cape*,<sup>44</sup> where a parent company was found to have 'assumed responsibility' for the employees of the subsidiary on the basis *inter alia* of the superior knowledge of the parent company on which the subsidiary was entitled to rely for handling asbestos risks for the employees.<sup>45</sup> A recent decision from the Supreme Court of the United Kingdom (UKSC)<sup>46</sup> makes clear that the central element in the Chandler decision was indeed the 'assumption of responsibility' and that the

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Delaware 4 May 2016, *Abdur Rahaman v. Jenny Penney Corporation, Inc.*, C. A. No. N15C-07-174 MMJ. In Germany, a supply chain liability case (the KIK case) has been rejected in January 2019 on the basis that the time limitation had expired, see [www.business-humanrights.org/en/kik-lawsuit-re-pakistansuit](http://www.business-humanrights.org/en/kik-lawsuit-re-pakistansuit).

- 41 On the applicability of the concept of vicarious liability in groups of companies and supply chains, see V. ULFBECK & A. EHLERS, 'Tort Law, Corporate Groups and Supply Chain Liability for Workers' Injuries: The Concept of Vicarious Liability', 13. *ECL (European Company Law)* 2016(5), p 167. On groups in particular, see C. WITTING, *Liability of Corporate Groups and Networks* (Cambridge University Press 2018).
- 42 EUROPEAN GROUP ON TORT LAW (EGTL), *Principles of European Tort Law: Text and Commentary* (2005), p 86: 'In other words: an omission ... can be considered as wrongful and faulty only if there is a norm which states a duty to act and to take care'.
- 43 M. PETRIN, 'Assumption of Responsibility in Corporate Groups: *Chandler v. Cape plc*', 76. *MLR (Modern Law Review)* 2013, pp 603, 614 and . 74. The term 'gap-filler' is used to highlight the fact that the claim demands a special legal construction in order to be justified. The term is not used as equivalating general 'default rules'.
- 44 Court of Appeal 25 April 2012, *Chandler v. Cape plc* (2012) EWCA Civ. 525. For an analysis see M. PETRIN, 76. *MLR* 2013, p 603. See also E. MCGAUCHEY, '*Donaghue v. Salomon* in the High Court', 4. *JPIL (Journal of Personal Injury Law)* 2011, p 249; P. ROTT & V. ULFBECK, 'Supply Chain Liability of Multinational Corporations?', 23. *ERPL (European Review of Private Law)* 2015(3), pp 415.
- 45 Decision para. 78. The criterion of 'reliance' was also central in a similar Canadian case, Ontario Superior Court *Choc v. Hudbay Minerals Inc.*, [2013] O.J. No. 3375, 2013 ONSC 1414.
- 46 Supreme Court 10 April *supra* . 44.

Chandler decision should be viewed as an example of how a sufficiently tight control on the part of the parent company can be established in order to create an assumption of liability.<sup>47</sup> In line with this, it has been argued that the assumption of liability test would also be applicable in supply chains based on contracts if control by the lead company is sufficiently tight.<sup>48</sup> The argument was tried out in the Canadian case *DAS v. George Washington*,<sup>49</sup> concerning the Rana Plaza disaster in Bangladesh, where it was argued that the lead firm in Canada, Lobwas, had assumed responsibility for the safety of the workers employed by a supplier's supplier (New Wave) in Bangladesh *inter alia* by incorporating its CSR standards into the supply chain contracts and by retaining the ability to cancel orders in case of non-compliance with these standards (control).<sup>50</sup> The Supreme Court did not rule out that there could be liability but rejected the concrete case on the basis that – under Bangladeshi law which was the governing law – it could not be established with sufficient likelihood that the lead company could be held liable for the acts of the supplier.<sup>51</sup>

This aspect of the case connects to the other basic problem in applying tort law outlined above, which is that outsourcing practices may also have as a consequence that damage causing activities take place in societies with a lower level of social and environmental protection. This raises the question whether tort law can be used to enforce voluntarily undertaken CSR policies. As a starting point, policies that are voluntarily undertaken by certain companies cannot be considered as general tort law standards, but must be regarded as ethical standards to which a company has chosen to adhere. Consequently, CSR standards would not be relevant for the shaping of tort law duties. However, there are a number of exceptions to this general rule. Firstly, if it can be established that living up to certain CSR standards can be regarded an industry practice it may be possible to argue that the standards are relevant for determining the standard of care in tort law.<sup>52</sup> Secondly,

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47 Decision paras 59–61. Lord Briggs further emphasized that there was ‘nothing special or conclusive about the bare parent/subsidiary relationship’ and that ‘the general principles which determine whether A owes a duty of care to C in respect of the harmful activities of B are not novel at all’, decision para. 54.

48 P. ROTT & V. ULFBECK, 23. *ERPL* 2015, p 434; C. TERWINDT, ‘Supply Chain Liability: Pushing the Boundaries of the Common Law?’, 8. *JETL (Journal of European Tort Law)* 2017(3), pp 261–296, 280–281.

49 Ontario Court of Appeal 20 December 2018, *supra* . 44.

50 On the interplay between contract and tort in supply chains, see V. ULFBECK & O. HANSEN, ‘Interplay between Contract and Tort in the Supply Chain’, in V. Ulfbeck, A. Andhov & K. Mitkidis, *Law and Responsible Supply Chain Management – Contract and Tort, Interplay and Overlap* (Routledge 2019), p 133.

51 Paragraph 176.

52 C. GLINSKI, ‘The Ruggie Framework, Business Human Rights, Self-regulation and Tort Law: Increasing Standards by Mutual Impact and Learning’, 35. *NJHR (Nordic Journal of Human Rights)* (1), pp 15, 28; C. WITTING, *Liability for Negligent Misstatements* (Oxford University Press

in some situations it may also be possible to argue that a company is bound by its own standard so that such ‘individual self-regulation’ can be accepted as forming tort law duties for that particular company.<sup>53</sup> Thirdly, even more complicated constructions such as ‘interference with third party rights’ and ‘protection of incidental third parties through tort law’<sup>54</sup> have been scrutinized in order to establish a basis for a tort law claim against the lead company for infringements of its CSR policy.

This all points in the direction that even tort law is challenged in protecting social goals under today’s business models. The overall picture is that it is necessary to rely on the application of special ‘gapfillers’ and exceptions to the general principles of tort law rather than the general rules.<sup>55</sup>

In addition to the challenges described above, both contract law and tort law assessments may be further complicated by the interplay between the role played by the leadfirm as a ‘regulator’ and private implementers (certifiers) of common CSR policies in the supply chain (see further below under 2.3.). Thus, with regard to the CSR clauses in the contracts, the way in which CSR policies are implemented at the more detailed level in the supply chain may also affect the interpretation of the clauses and thereby their regulatory effect in contracts. With regard to tort law liability, the Das-case shows that the role played by the social auditor may also potentially affect the liability of the leadfirm as a regulator. Thus, in this case it was argued that Lobwas had assumed responsibility by engaging Bureau Veritas to conduct social audits and furthermore that this engagement had created reliance by workers who saw Bureau Veritas’ personnel conducting the audits. The involvement of a certifier may also raise the question of the extent to which the chain leader may rely on the assessments made by this third party and whether this could lead to a lowering of the level of awareness required by the chain leader.<sup>56</sup> Thus, the interplay between standard setting and certification may add a further layer of complication to the liability assessment.

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2004), p 252 on how professional bodies may have the power to determine industry practice for a given profession.

- 53 C. GLINSKI, 35. *NJHR*, pp 15, 27; A. BECKERS, *Enforcing Corporate Social Responsibility Codes*, p 177 with further references. See also the Danish case Østre Landsret 13 September 2008 reported in the Danish Weekly Law Reports as UfR 2008.70 Ø.
- 54 V. ULBECK & O. HANSEN, in *Law and Responsible Supply Chain Management*, p 137 with further references.
- 55 Similarly, it is observed in P. VERBRUGGEN, 27. *ERPL* 2019, p 319, that with regard to liability of private standardization bodies, tort law presently can only play a limited role in including ‘good governance’ principles in liability assessments. The author further makes reference to J. BEERMANN, ‘The Reach of Administrative Law in the United States’, in M. Taggart (ed.), *The province of Administrative Law* (Hart Publishing 1997), pp 171, 187 stating that negligence actions against SDOs ‘resemble a weak form of administrative and due process law’.
- 56 C. GLINSKI & P. ROTT, 23. *DLR*, 2018, pp 83, 114.

### 2.3. *Implementation: Private Certification*

The incorporation of CSR obligations in the contracts and in the codes of conduct in the supply chain is often combined with an ongoing control and supervision with the implementation of the CSR principles by the suppliers in the chain. Control and supervision of private actors performing tasks of public interest is normally regarded a public task and has largely been undertaken by the executive, sometimes by way of certification.<sup>57</sup> The task of certifying is sometimes delegated from public authorities to private actors.<sup>58</sup> In these cases the certifiers carry out the task on behalf of the public authority and on the basis of statutory regulation.<sup>59</sup> However, in the supply chain context certification is often carried out on a purely private basis, for instance by the chain leader entering into a contract with the certifier for the monitoring and control of their supply chains with regard to various standards concerning the environment and workplace conditions.<sup>60</sup> If the certifiers are not accredited by a public authority no public authority stands behind or is accountable for these voluntary certifications. Private certification in the supply chain therefore raises the basic question whether accountability as a public interest can be safeguarded by private law liability rules.<sup>61</sup> Since third parties are the real beneficiaries of the certification, a central question is the possible liability of the private certifier towards third parties suffering injuries in situations where the certification is flawed.

However, establishing tort law liability towards third parties may prove difficult. The problem is that the duty of the certifier is solely based on the contract between the certifier and the chain leader (or the supplier), whereas a tort law duty would need to be based on general norms that are independent of a

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- 57 On certification in general, see P. ROTT (ed.), *Certification – Trust, Accountability and Liability* (Springer 2019); J. BELSON, *Certification and Collective Marks* (Edward Elgar Publishing 2017). For liability of social auditors in particular, see T. VAN HO & C. TERWINDT, 27. *ERPL* 2019, pp 379–402.
- 58 As to public security as a public task that can be transferred to private actors acting as certifiers, see C. GLINSKI & P. ROTT, 23. *DLR* 2018, p (83) at 85: ‘These certification bodies remove from the state the burden of performing the relevant duties through public authorities’.
- 59 These situations can be classified as state driven private governance. Liability of the certifier can often be based on statutory framework establishing the duty of care of the public authority, which has been delegated to the private certifier, C. GLINSKI & P. ROTT, 23. *DLR* 2018, pp 83, 92, referring to the example vehicle certification by private actors.
- 60 C. GLINSKI & P. ROTT, 23. *DLR* 2018, pp 83, 110. A parallel can be found in the financial market where it is common for companies to be rated, either on the initiative of a rating agency (unsolicited rating) or based on a contract between the company and a rating agency (solicited rating) although there is no public law requirement to do so.
- 61 C. GLINSKI & P. ROTT, 23. *DLR* 2018, pp 83, 86: ‘In economic terms, legal liability for insufficient control and for certification without the relevant requirements being met, is an important mechanism to avoid dysfunctional incentives, resulting from the relationship between the certifier and the certified entity’.

contract. Third party liability of private auditors is well known in cases where there is a statutory basis for the task undertaken by the private auditor (state driven private certification) who is then most often subject to a professional liability standard. Liability of accountants is a clear example. The situation discussed here differs from these situations in that the certifier has not by statute (and thereby society) been officially recognized as an expert.<sup>62</sup> The problem with purely contract based certification was illustrated in the Canadian case *DAS v. George Washington*<sup>63</sup> discussed above. In this case, the tort law claim against Bureau Veritas was rejected on the basis that the social auditing contract with Lobwas did not contain a duty to inspect the building in which the employees were working. Thus, the case implicitly acknowledges that contrary to the general principle of privity of contract it may be necessary to rely on the contract between the parties to establish a tort law duty towards third parties. Also in English law, it would be necessary to apply special tort law rules, for example on assumption of responsibility in order to establish liability on the part of the certifier.<sup>64</sup>

As an alternative to tort liability, plaintiffs may attempt to rely on contract law. As a starting point, however, also here the doctrine of privity of contract would bar a claim raised by the injured party. Consequently, it would be necessary to rely on exceptions to this doctrine as a basis for a claim. In German law, the concept of the ‘contract with effect for third parties’ has been relied upon in cases concerning certifier liability in other areas of the law.<sup>65</sup> The doctrine entails an ‘objective, normative, complementary interpretation of the actual agreement in the light of the principle of good faith’.<sup>66</sup> The protection of third parties may be included in the purpose of the contract even where this is not clearly in the interest of one of the parties. These criteria bring the contract with protective effect close to tort law

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- 62 Also T. VAN HO & C TERWINDT, 27. *ERPL* 2019, pp 379, 391 observe the difficulties in relying on case law concerning financial auditing for establishing liability of social auditors.
- 63 On Ontario Court of Appeal 20 December 2018, *supra* . 44.
- 64 T. VAN HO & C TERWINDT, 27. *ERPL* 2019, pp 379, 386–387 identifying three possible liability tests: (1) *The Caparo Industries v. Dickmann test*, specifically developed for ‘novel’ liability situations, (2) the incremental approach and (3) the assumption of liability test. See also above s. 2.2 on regulation.
- 65 This has been the case in the area of maritime law, see the case Oberlandesgericht Hamburg 6 U 34/90 14 June 1990, reported in [1991] *Versicherungsrecht (VersR)* 476. However, most often actions on this basis have been unsuccessful as it has not been possible to show that the third party belonged to a protected class, see further J. BASEDOW & W. WURMNEST, ‘Klassifikationsverträge als Verträge mit Schutzwirkung zugunsten Dritter’, *VersR* 2005, p 328; V. ULFBECK & A. MÖLLMANN, ‘Public Function Liability of Classification Societies’, in P. Rott (ed.) *Certification: Trust, Accountability and Liability* (Springer 2019) (forthcoming) pp 213 – 229. With regard to ratings in the financial markets, see A. HALFMEIER, ‘Die Haftung von Ratingagenturen gegenüber Kapitalanlegern: Von Sydney lernen?’, 9. *VuR* 2014, concerning liability of rating agencies.
- 66 C. GLINSKI & P. ROTT, 23. *DLR* 2018, pp 83, 88.

reasoning and the construct is often seen as in reality belonging to tort law or as serving a gap filling function between contract and tort.

Also with regard to establishing liability of the certifier there will often be an interplay between the implementation function of the certifier and the rule making function of the lead firm. Thus, in German law, it has been argued that in the case of purely voluntary certification a duty of care on the part of the certifier *vis-à-vis* third parties can only arise if this duty has been delegated from the chain leader to the certifier.<sup>67</sup> This in turn requires that the chain leader is itself under a duty of care towards third parties. Likewise, a third party protective effect of a contract can *inter alia* be found if one of the contracting parties is responsible for the well-being of a third party.<sup>68</sup> Consequently, with regard to supply chain certification, it seems likely that establishing a duty of care towards third parties on the part of the chain leader could trigger a basis of liability also for the certifier under the doctrine of contracts with protective effects for third parties.<sup>69</sup> However, establishing a basis of liability is not enough. It is also necessary to establish causation. In other words, it is necessary to show that the detection of risks to health and safety by the certifier would enable the mitigation of those risks, through the influence that the chain leader can have on the supplier. In other words, establishing liability of the certifier (column 2) might well require an analysis of the extent of the contractual control exercised by the rule making chain leader over the parties in the supply chain (column 1).

In sum, also the phenomenon of private certification seems to require the application of primarily specific ‘gap filling’ rules and exceptions to the general rules of tort law and contract law if private law is to function as a tool for establishing certifier accountability.<sup>70</sup> In addition, it seems that whether the claim is based

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67 C. GLINSKI & P. ROTT, 23. *DLR* 2018, pp 83, 104-105, 113. The argument is based on the rationale that the certifier would not have an original duty of care as it neither created a risk nor is it originally responsible for the safety of the factory.

68 C. GLINSKI & P. ROTT, 23. *DLR* 2018, pp 83, 89.

69 In legal theory it has been argued that establishing such a duty of care on the part of the chain leader must be regarded a prerequisite for establishing liability of the certifier, see C. GLINSKI & P. ROTT, 23. *DLR* 2018, pp 83, 114.

70 The widespread use of private certifiers may also challenge private law concepts in another way. This is evidenced by a line of cases that have been presented in the US concerning the liability of credit rating agencies. For a short historic account, see E. NÅSTEGÅRD, *Credit rating agencies and the First Amendment defence in the US* (Nordic and European Company Law Working Paper No. 16-17 2017). In these cases, the rating agencies have raised it as a defense against tort liability that their ratings were protected by the first amendment on freedom of speech as expressions of opinion comparable to journalistic expressions. For a period of time, the courts accepted this argument, in cases where ratings has such a character that they could be considered to be of ‘public concern’ and in particular in cases of unsolicited ratings. See for instance U.S. District Court for the Central District of California 18 March 1999, *County of Orange v. McGraw Hill Companies, Inc*, 245 B.R. 151; U.S. Supreme Court 21 June 1990, *Milkovich v. Lorain Journal Co*, 497 U.S.1. The rating

on tort law or contracts with protective effects for third parties, establishing liability of the certifier (column 2) may well involve establishing liability of the chain leader (column 1) as a prerequisite.

#### **2.4. *Dispute Resolution: Mediation***

If a dispute arises concerning CSR commitments or certifiers' liability, legal adjudicative processes (such as litigation and commercial arbitration) are generally available only to a party who can establish a relevant claim and cause of action. As shown in section 2.2, CSR commitments often do not create legal (enforceable) obligations and even if they do, remedies may be unavailable. In many situations, parties in the supply chain as well as third parties will thus be unable to establish a relevant claim and cause of action in cases of non-compliance with CSR commitments. As shown in section 2.3, flawed certifications will often not provide affected third parties with any cause of action against the certifier. Even if there is a basis for raising a relevant claim, some jurisdictions prevent private actors from enforcing CSR commitments *vis-à-vis* other private actors, if such CSR commitments reflect existing legal obligations under public (statutory) law that safeguard general public interests and are subject to public enforcement by the state.<sup>71</sup> Moreover, adjudicative processes do not support the relational character of the contract described in section 2.2. On this background, a consensual process such as mediation can be an attractive alternative means of dispute resolution in the supply chain.<sup>72</sup>

Mediation is a voluntary dispute resolution process in which a neutral third party (the mediator) helps the disputing parties to find a mutually satisfactory solution to their dispute (a settlement). In many jurisdictions, mediation is not subject to any detailed statutory regulation.<sup>73</sup> Instead, numerous soft law standards

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agency cases illustrate how private governance situations may force considerations of the applicability of public law notions in private law and how private law reasoning can be challenged - or maybe even short circuit - by such notions.

- 71 Under Danish law, private actors do not in general have legal standing to enforce such public law rules in civil litigation, and this also affects the arbitrability of disputes that, in effect, aim for such enforcement, see judgment from the Danish Supreme Court 17 February 1999, reported in the Danish Weekly Law Reports as UfR 1999.829 H.
- 72 See e.g. C. REES, *Mediation in Business-Related Human Rights Disputes: Objections, Opportunities and Challenges* (Corporate Social Responsibility Initiative Working Paper No. 56. Cambridge, MA: John F. Kennedy School of Government, Harvard University 2010). Mediation plays a key role in the national contact points' handling of alleged non-observance of the OECD Guidelines for Multinational Enterprises (2011).
- 73 UNCITRAL has adopted the Model Law on International Commercial Conciliation (2002), recently replaced by the Model Law on International Commercial Mediation and International Settlement Agreements Resulting from Mediation (2018), which provides uniform rules in respect of basic principles for the mediation process. In the EU, the Mediation Directive (2008/52/EC) addresses a

for mediation have emerged which seek to safeguard fundamental ‘procedural justice values’.<sup>74</sup> Mediation is thus a form of private governance that originates from the market and is subject to general rules of private law. Unlike dispute resolution processes of an adjudicatory nature, a mediator cannot impose any decision on the parties. Instead, mediation supports the autonomy of the parties to make their own decisions about the dispute. Mediation can be performed in many different ways, and many mediators develop their own models or concepts.<sup>75</sup> In most jurisdictions, anyone can provide mediation as a service.

Mediation as a means of dispute resolution is not limited to ‘legal disputes’, and it is thus possible to mediate disputes concerning CSR commitments regardless of how they are qualified. However, the ability of mediation to support compliance with CSR commitments seems limited for at least two reasons. First, since the mediator cannot impose any decision on the parties, the outcome of any mediation will depend entirely on the mutual will of the disputing parties at the time of disputing.<sup>76</sup> Secondly, mediation is strongly focused on the individual interests and needs of the parties, including the relation between the parties. This makes commercial mediation well-suited to support the relational character of the contractual relation between the parties mentioned in section 2.2, whereas mediation (in its usual forms) is generally not suited to handle disputes involving separate interests of non-represented third parties.<sup>77</sup> Consequently, mediation can normally support compliance with CSR commitments only if the third parties affected by non-compliance with CSR commitments (or representatives of such third parties, e.g. NGOs) are properly involved in the mediation.<sup>78</sup>

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few aspects of mediation in cross-border civil and commercial matters, whereas the ADR Directive (2013/11/EU) addresses certain aspects concerning ADR of consumer disputes. Some jurisdictions (including Austria and France) have enacted more comprehensive state regulation of mediation and the practice of mediators. For a comparative overview of many European (and other) jurisdictions, see K.J. HOPT & F. STEFFEK, *Mediation: Principles and Regulation in Comparative Perspective* (Oxford: Oxford University Press 2013).

74 See e.g. the ICC Mediation Rules (2014), the European Code of Conduct for Mediators (2004) and the UNCITRAL Conciliation Rules (1980). Several arbitration and mediation institutions have also adopted their own rules.

75 For an overview, see e.g. L. RISKIN, ‘Understanding Mediators’ Orientations, Strategies and Techniques: A Grid for the Perplexed’, 7. *HNLR (Harvard Negotiation Law Review)* 1996, pp 9 et seq.; V. VINDELØV, *Reflexive Mediation: With a Sustainable Perspective* (DJØF 2012).

76 On the free will of the parties as an essential element of mediation, see e.g. K.J. HOPT & F. STEFFEK, *Mediation*, p 12.

77 Even though there are examples of mediation models giving a higher priority to harmony and community values than the interests of the individual, see V. VINDELØV, *Reflexive Mediation*, p 45.

78 Under the OECD Guidelines for Multinational Enterprises (2011), there are several examples of successful mediations, including third parties, by national contact points, see [mneguidelines.oecd.org/](http://mneguidelines.oecd.org/).

At the more general level, it seems that mediation as a means of dispute resolution creates challenges in private law that are similar to those identified *supra* 2.2 and 2.3. We will here highlight two.

The first challenge is related to the contractual effects between the parties to the conflict of a mediation clause in the contract. In several cases, common law courts have denied to enforce such mediation agreements comparing them with agreements to agree and agreements to negotiate in good faith, which are generally unenforceable.<sup>79</sup> However, some recent decisions from common law courts uphold mediation clauses as enforceable contracts, if specific duties of the parties in the mediation can be sufficiently established.<sup>80</sup> In such situations, it remains a challenge to determine the requirements for ‘specific performance’ of a mediation agreement: How (and for how long) is a party to a mediation agreement expected to take part in a mediation in good faith, acknowledging that the party has no obligation to reach a settlement of the dispute?<sup>81</sup> Apart from specific performance, a party in breach of its obligations under a mediation agreement can, in principle, also incur a liability in damages. However, it seems difficult to assess the economic loss suffered by the other party, because there is obviously no guarantee that a correctly performed mediation would have resulted in a mutually satisfactory settlement agreement.<sup>82</sup> Thus, mediation does not invite a straight forward application of general private law rules as a tool for enforcement.

The second challenge in private law concerns regulating the role of mediators. As mentioned, the role of mediators (and the concept of mediation) remains largely unregulated in many jurisdictions which makes it difficult for private law to

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79 Several common law courts have traditionally adopted this approach. For an overview of relevant case law, see P. BROOKER, *Mediation Law: Journey through Institutionalism to Juridification* (Routledge 2013), pp 42–82.

80 To enforce mediation agreements, some courts and arbitrators have been willing to either dismiss a complaint as (currently) inadmissible or to stay the proceedings, until the parties have performed their obligations to mediate, see *ibid.* However, the predominant finding from a comparative perspective is that a mediation agreement is no obstacle to litigation or arbitration under procedural law, see K.J. HOPT & F. STEFFEK, *Mediation*, p 37.

81 Many jurisdictions have considerable difficulties with specifying the obligations of the parties, see K.J. HOPT & F. STEFFEK, *Mediation*, p 63. A number of more specific duties have been established in German law, see *ibid.*, pp 63, 549; S. RÜTZEL, G. WEGEN & S. WILSKE, *Commercial Dispute Resolution in Germany* (Beck C. H., 2nd edn 2016), p 199. The UNICTRAL Model Law on International Commercial Mediation and International Settlement Agreements Resulting from Mediation (2018) proposes the following statutory regulation in Art. 14: ‘Where the parties have agreed to mediate and have expressly undertaken not to initiate during a specified period of time or until a specified event has occurred arbitral or judicial proceedings with respect to an existing or future dispute, such an undertaking shall be given effect by the arbitral tribunal or the court until the terms of the undertaking have been complied with, except to the extent necessary for a party, in its opinion, to preserve its rights. Initiation of such proceedings is not of itself to be regarded as a waiver of the agreement to mediate or as a termination of the mediation proceedings’.

82 See K.J. HOPT & F. STEFFEK, *Mediation*, p 64.

establish more precise duties of mediators (unless specifically regulated in the mediator contract) as well as to establish the applicable standard of care.<sup>83</sup> Furthermore, it can also be difficult to establish the necessary causal link between the mediator's breach of the standard of care and the loss to a disputing party, as well as adequacy.<sup>84</sup> In some jurisdictions, legislation and case law even protect mediators from civil liability, which reflects the presumption that facilitating settlement is part of a mediator's 'official capacity' that can be analogized to the judicial function.<sup>85</sup> In sum, private law seems to have significant challenges in regulating the role of mediators, and liability clearly seems to remain an exception in many jurisdictions.<sup>86</sup>

## 2.5. Conclusions

### 2.5.1. Cross-Column Observations

The examples above illustrate the phenomenon of private governance with regard to regulation, implementation and dispute resolution in global supply chains. The examples can be used for showing that a full private law analysis of a private governance system may necessitate looking across the 'columns'. This is true both with regard to the contractual relationship between the chain leader and the supplier and with regard to third party claims.

Thus, in the supply chain, codes of conduct can be seen as a regulatory framework (private regulation) governing the companies in the chain. To make the codes operational, they are often incorporated into the contracts in the chain. However, the enforcement of the contract is not entirely left to the parties. Often third party certifiers control and supervise the implementation of the standards. With regard to the contractual relationship between the parties, this raises the question to what extent the interpretation of the CSR clauses in the contract can be influenced by the understanding and implementation at a more detailed level of the standards by the certifier and also whether certification of the supplier by the certifier in it self can be raised as a defence by the supplier against the chain leader in a case concerning breach of the CSR commitments by the supplier.

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83 See K.J. HOPT & F. STEFFEK, *Mediation*, pp 74-77; A. EHLERS, 'Blaming the Unblameable: On the Liability of Mediators', 1. *NJCL (Nordic Journal of Commercial Law)* 2014, pp 1-33. In some jurisdictions, more precise duties seem to exist. See e.g. on German law F. HAFT & K. GRÄFIN VON SCHLIEFFEN, *Handbuch Mediation* (C.H.Beck, 3rd edn 2016), pp 635-647. Mediator contracts rarely provide an elaborate description of the mediator's services, see e.g. M. MOFFITT, 'Suing Mediators', 83. *BULR (Boston University Law Review)* 2003(147), pp 163-167.

84 *Ibid.*

85 For details, see C. CHERN, *International Commercial Mediation (Dispute Resolution Guides)* (Informa Law from Routledge 2008), pp 229-232.

86 As noted by A. EHLERS, 1. *NJCL* 2014, p 3, 'it is uncommon that practically all of the basic liability requirements will give rise to problems'.

However, as described above, the inclusion of CSR clauses as regulatory tools in the contract also turns the contractual relationship into a more ‘relational contract’. Consequently, should a dispute arise between two parties in the supply chain, the parties are likely to attempt to solve their dispute informally or by mediation. In these situations, private law may have less to offer in solving CSR issues between the parties, although the obligations are found in contracts. Rather, private law issues may be ‘transferred’ to the level of dispute resolution and concern the enforceability of mediation clauses and/or the possible liability of the mediator.

With regard to third party claims, these may be raised both against the chain leader and the certifier. However, the analysis shows that evaluating the possible liability of the certifier *vis-à-vis* third parties may require an evaluation of the extent to which the rule maker, i.e. the chain leader, itself has a duty of care towards the third party. The use of certification also raises the question whether the required level of awareness on the part of the chain leader may be lowered if a certifier is involved. Moreover, to the extent both the chain leader and the certifier can be held liable towards a third party, liability may be shared and apportioning liability between the two will require looking at the collaboration between them as a whole.

### 2.5.2. *Market-Driven Private Governance: An Exception-Based Private Law*

The example of global supply chains focuses on situations in which private governance initiatives have been initiated in the market (marketdriven). Our analysis shows that in *all of the examples* of private governance emerging from the market both contract law and tort law are challenged if they are to serve as enforcement mechanisms. Moreover, the challenges seem to be of a similar nature across the different functions in the governance system. The most pertinent question is to what extent private law can safeguard public interests or public values in these private governance models. In this regard, our analysis shows that private law may be ill equipped to handle the pursuance of public values and interests by private actors. Thus, as a starting point public values, representing external interests, are a stranger to contract law. Even tort law, although concerned with the protection of third party interests in a broader sense, is challenged when it comes to protecting these interests in the employed business models. Consequently, only by use of rules and principles that in private law are thought of as *exceptions* to general rules, such as third party beneficiary law, reliance based liability, innovative principles of interpretation and specific gap filling rules is it possible to find mechanisms in private law that can protect the public values at stake in private governance systems. In this sense, the phenomenon of private governance can be seen as relying on an ‘exception-based’ private law in the safeguarding of public values and interests.

### 3. Private Governance Emerging from the State: The Example of Outsourcing of Universal Services

#### 3.1. Introduction

Traditionally, European states and local governments have been extensively involved in markets for supply of universal services, such as energy and communication.<sup>87</sup> Furthermore, production and supply companies were often vertically integrated and organized in such a way that they legally or practically acted as monopolies *vis-à-vis* the end users.<sup>88</sup> By the end of the 20<sup>th</sup> century, these markets were ‘liberalized’ within the EU. Supply and distribution monopolies were dissolved and public entities largely withdrew from previous ownership.<sup>89</sup> The aim of liberalization was to increase efficiency by establishing private, competitive markets for universal services, but to secure production, distribution and supply of universal services in accordance with public values and interests as well.<sup>90</sup> Thus, market behaviour in these sectors is widely regulated by legislation at EU – and national level. The regulation of the energy sectors within the EU seems to serve as one prominent European example of an attempt to implement public values into private markets (‘publicization’<sup>91</sup>).

In the following, we will use EU regulation, national Danish and German law and examples of contract clauses in a cross-column analysis to show how state-driven private governance systems function as regulators, implementers and dispute resolution bodies. This analysis will illustrate how state driven private governance challenges private law.

#### 3.2. Regulation: EU-Based Statutory Law and a Limited Role of Private Contracts

In the energy sector, the primary means for liberalization has been a legal unbundling of the previously vertically organized production, transmission and distribution

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87 See e.g. U. COLLIER, ‘Local Energy Concepts in Germany – An Environmental Alternative to Liberalisation?’, 5. *E&E (Energy & Environment)* 1994(4), p 311; B.O.G. MORTENSEN, *Elforsyning: Afvejning af hensyn i en sektor på vej mod det indre marked* (DJØF 1998), p 178; J. MUNKSGAARD, J. RAMSKOV, A. KARSEN & P. FRISTRUP, *Gasmarkedet i Danmark – fra monopol til konkurrence* (AKF 2004), p 26.

88 See e.g. U. COLLIER, 5. *E&E* 1994(4), p 311; B.O.G. MORTENSEN, *Elforsyning*, pp 34, 167-174.

89 See J. MUNKSGAARD, J. RAMSKOV, A. KARSEN & P. FRISTRUP, *Gasmarkedet i Danmark*, pp 28-30.

90 See e.g. Art. 1 of the EU Electricity Directive, Dir. 2009/72 of 13 July 2009 concerning common rules for internal market in electricity and repealing Directive 2003/54/EC, data.europa.eu/eli/dir/2009/72/oj.

91 See J. FREEMAN, 116. *HLR* 2003, pp 1285-1352 and s. 1.3., *supra*.

of electricity and gas.<sup>92</sup> However, public interest in energy supply has entailed the establishment of intensive control of the liberalized markets at various levels of the supply chain and by way of different methods. Production and partly also the supply of energy resources require concession.<sup>93</sup> Distribution tariffs or pricing methodologies may be fixed or approved by national energy authorities.<sup>94</sup> Private energy supply businesses must largely display prices and conditions to the public.<sup>95</sup> They must offer their services to all customers in accordance with fundamental principles of a public law nature<sup>96</sup> and – in many situations – to any customer requiring them.<sup>97</sup> Within the EU, member states and private energy companies are under an obligation to secure a certain level of consumer protection in national legislation and contractual practices.<sup>98</sup> Furthermore, national energy authorities can set aside prices and conditions even in the relations between energy companies and business customers,<sup>99</sup> e.g. if these are considered to be unfair or if such interference is needed to avoid ‘environmentally and socioeconomically inappropriate use of energy’.<sup>100</sup>

Indeed – in addition to this detailed sector regulation – contracts entered into by e.g. private energy supply companies and their customers (i.e. the end users) still define some of the conditions for the supply. Thus, these contracts take the shape of regulation as well. However, the described legislative framework – intervening at various stages of transactions – in many situations leave a very narrow space for the autonomous formation of contracts between the supply companies and the end users<sup>101,102</sup>, and – as we will show in the following – impact significantly on their legal effects.

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- 92 P. CAMERON & R. HEFFRON (eds), *Legal Aspects of EU Energy Regulation* (Oxford: Oxford University Press, 2th edn 2005), p 17.
- 93 See Arts 7 and 10 of Dir. 2009/72; § 10 and § 19 of the Danish Electricity Supply Act (*lov om elforsyning*); § 4 and 4a of German Energy Industry Act (*Energiewirtschaftsgesetz*).
- 94 See e.g. Art. 37, subs. 1(a) of Dir. 2009/72; § 69 of the Danish Electricity Supply Act (*lov om elforsyning*) on the use of a governing revenue framework (*indtægtsramme*) as price control mechanism.
- 95 See e.g. Art. 3, subs. 3, of Dir. 2009/72; § 76, subs. 1, of the Danish Electricity Supply Act (*lov om elforsyning*); § 5a and § 36 of German Energy Industry Act (*Energiewirtschaftsgesetz*).
- 96 See e.g. Art. 1 of Dir. 2009/72; § 6d of the Danish Electricity Supply Act (*lov om elforsyning*); § 10e the German Energy Industry Act (*Energiewirtschaftsgesetz*).
- 97 See below in s. 3.3.
- 98 See e.g. Arts 1 and 3 and Annex 1 of Dir. 2009/72.
- 99 See e.g. Art. 37, subs. 10 of Dir. 2009/72.
- 100 See e.g. § 77, subs. 3 of Danish Electricity Supply Act (*lov om elforsyning*).
- 101 See P. MUSSAEUS, I. RAUSCH & M. MORAING (eds), *Verträge der Energiewirtschaft: Strom, Gas, Erneuerbare Energien, KWK* (De Gruyter 2014), p 175.
- 102 Standard conditions for the supply of e.g. electricity are widely made public on the different suppliers’ websites. In comparison, they seem to contain only few variations.

### 3.3. *Implementation: The Private Provision of Universal Services*

One prominent tool for the described ‘publicization’ of energy markets is the obligation often placed upon private supply companies to offer their services to any customer demanding them, i.e. an obligation to supply. Such obligation may follow expressly from EU or national legislation. For instance, according to Article 3 of the EU Electricity Directive, member states can place upon private electricity producers and system operators ‘public service obligations’ (subs. 2), including an obligation to supply consumers and small enterprises (subs. 3). Consequently, according to § 6 b of the Danish Electricity Act, private companies that offer electricity products within a given area, are under a duty to offer these products to all ‘consumer households’.<sup>103</sup>

An obligation to supply may also follow *indirectly* - from those general duties of public law nature which are placed upon the private suppliers as a precondition for any market activity. Within the EU, energy supply companies are obliged to offer their services on the basis of ‘transparent, objective, fair and non-discriminating conditions’.<sup>104</sup> Thus, because of this general principle, private energy suppliers may have an obligation to supply to *any* customer demanding their services, i.e. including business customers. At least it may considerably reduce the possibilities for the supplier to reject a customer.<sup>105</sup>

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103 See e.g. also Art. 3 of the EU Gas Directive, Dir. 2009/73/EC of the European Parliament and of the Council of 13 July 2009 concerning common rules for the internal market in natural gas and repealing Directive 2003/55/EC, [data.europa.eu/eli/dir/2009/73/oj](http://data.europa.eu/eli/dir/2009/73/oj), and corresponding national legislation, cf. the Danish Act on the Supply of Natural Gasses (*Naturgasforsyningsloven*), § 7. According to Art. 4 of the Universal Service Directive, the member states shall ensure ‘that all reasonable requests for connection at a fixed location to the public telephone network and for access to publicly available telephone services at a fixed location are met by at least one undertaking’, cf. also the Danish Act on Telecommunication (*Teleloven*), §§ 3–6. Comparable rules are found in Art. 3 of the EU Postal Directive (EU Dir. 1997/67 on common rules for the development of the internal market of community postal services and the improvement of quality of service, [data.europa.eu/eli/dir/1997/67/oj](http://data.europa.eu/eli/dir/1997/67/oj)). At national level, an obligation to contract or a supply duty may also lie with e.g. heating stations and water supply plants, cf. e.g. § 45 of the Danish Water Supply Act.

104 Article 3, subs. 1 of Dir. 2009/72; e.g. § 6d of the Danish Electricity Supply Act (*lov om elforsyning*).

105 An obligation to contract may also (indirectly) be a consequence of rules of competition law. General principles of competition law will generally include doctrines of non-discrimination, cf. e.g. EUT Art. 101 and Art. 102 and § 6 of the Danish Competition Law (*konkurrenceloven*), and can be regarded as (indirectly) imposing duties on the parties to the contract. The *contractual* nature of these principles of competition law is however generally unclear. Within the EU a breach of fundamental principles of competition law (such as restrictive or discriminating trade practices) will establish a basis for a claim for damages in accordance with general tort law principles, cf. Art. 3 of Dir. 2014/104 of 26 November 2014 on certain rules governing actions for damages under national law for infringements of the competition law provisions of the Member States and of the European Union, <http://data.europa.eu/eli/dir/2014/104/oj>, as implemented by § 3 of the

Often the duty to supply entails an obligation for the private supplier to enter into a *contract* with the end user.<sup>106</sup> However, such obligation to contract contradicts the fundamental principle of party autonomy in private law.<sup>107</sup> The lack of consent to the transaction may affect contract interpretation<sup>108</sup> but also more radically impact the applicability of general principles of contract law to the transaction. Thus, the legal character of such mandatory contracts may not be clear.

As an example, in some member states any supply of electricity requires an express contract to be entered into between the supply company and the end user.<sup>109</sup> Other member states place the general supply duty upon one supplier of

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Danish act on the Handling of Claims for Damages caused by Breach of Competition Law (*Lov om behandling af erstatningssager vedrørende overtrædelser af konkurrenceretten*) and § 33a of the German Act against Restriction of Competition (*Gesetz gegen Wettbewerbsbeschränkungen*). An obligation to contract may also be a possible consequence of an application of fundamental rights, cf. e.g. T. WILHELMSSON, 'Contract and Equality', 40. *SSL (Scandinavian Studies in Law)* 2000(145-165), p 153.

106 See e.g. the Danish Electricity Supply Act § 6 (*lov om elforsyning*) and (with respect to consumers) the Dir. 2009/72, Appendix I, s. 1a.

107 One prominent example of an attempt to merge these conflicting poles of public and private law is the Swiss Federal Court's decision of 7 May 2002, p 129, in *Post v. Verein gegen Tierfabriken*. In this case, the Federal Court found an obligation to contract as *embedded in contract law itself*, where a supplier's refusal to enter into a contract was considered as '*sittenwidriges Verhalten*'. The decision was widely criticized, however primarily for neglecting a direct applicability of fundamental rights as grounds for imposing a duty of non-discrimination, cf. e.g. Y. HANGARTNER, 'Bemerkungen zu BGE 129 III 35', 6. *AJP (Aktueller Juristische Praxis)* 2003, pp 690 et seq.; W. KÄLIN, R. KIENER, A. KLEY, P. TSCHANNEN & U. ZIMMERLI, 'Die staatsrechtliche Rechtsprechung des Bundesgerichts in den Jahren 2003 und 2004', 140. *ZBJV (Zeitschrift des Bernischen Juristenvereins)* 2004, pp 645 et seq.; M. CAMPRUBI, 'Kontrahierungszwang gemäss BGE 129 III 35: ein Verstoß gegen die Wirtschaftsfreiheit', 4. *AJP (Aktueller Juristische Praxis)* 2004, pp 384-404. More receptive towards a foundation of an obligation to contract within private law itself are however R. ARNET, *Freiheit und Zwang beim Vertragsabschluss* (Bern: Stämpfli Verlag AG 2007), pp 51 et seq., suggesting to regard the public offering of universal services like postal services as binding offers, and M. AMSTUTZ, A. ABEGG & V. KRAVAS, 'Civil Society Constitutionalism: The Power of Contract Law', 14. *Indiana Journal of Global Legal Studies* 2007(2), pp 235-258. In the Nordic countries, a foundation for an obligation to contract within private law has within *consumer contract law* been assumed by F. Nyberg, cf. F. NYBERG, *Avtalsfrihet - rätt till avtal, En nordisk undersökning om kontraheringsplikt till förmån för privatpersoner* (Nordiska ministerrådet 1997), pp 79, 230. In line with this, see also T. WILHELMSSON, 40. *SSL* 2000, p 164 and possibly also I. FALCH, *Rett til nett: Konkurransen i nettbundne sektorer* (Universitetsforlaget 2004), p 15.

108 T. INDÉN & K. N. OLESEN, 'The Public Sector and Obligation to Contract', 12. *ECLR (European Contract Law Review)* 2016(2), pp 87-93. The authors assume (however with considerable caution) that an obligation to contract may influence on contract interpretation. The authors conclude (pp 91 et seq.) that general principles of contract interpretation 'are fundamental with regard to forced contracts too, but as argued above there can be situations where they might be used with a twist'.

109 See e.g. § 6 of the Danish Electricity Supply Act (*lov om elforsyning*).

last resort, demanding no (express) contract between the end user and the supplier. In Germany, where the latter model is used,<sup>110</sup> the concluding or implied behaviour of the consuming end user will generally be considered as governed by the general rules of purchase in the Bürgerliches Gesetzbuch (BGB) (§§ 422 et seq.).<sup>111</sup> However the general principles of § 305 of the German BGB on the binding effect of standard form clauses into contracts under private law *does not* apply to the supplier of the last resort's terms conditions as these are regulated by law.<sup>112</sup> The stricter conditions of adhesion of § 305 BGB will apply in the case, where the supply of electricity (outside the scope of the supply duty of the supplier of last resort) is based upon (an express) contract, cf. § 41 of the German Energy Industry Act.

The link between the statutory supply duty and general principles of contract law may depend upon (on the one hand) the strength of the public values and interests involved and (on the other hand) the element of consent to the concrete transaction.

Without a mutual consent to the contract, one can ask whether parties may be bound to the terms of the agreement in the same way and under the same circumstances, as if the agreement were voluntary, and whether traditional remedies for breach will be available. For instance, the tight public regulative framework around the supply contract and the technical complexity of production, distribution and supply of energy will often bring about questions on the effect of changes in legislation on the rights and duties of the contracting parties. Due to the basic principle of freedom of contract, a *variation of the contract* needs in principle to be agreed upon, hereby fulfilling the same requirements as to formation as the original agreement.<sup>113</sup> However, public interests in the supply of the goods or services in question may lower the bars in contract law for accepting certain unilateral variations of the contract imposed by the supply company on its customers. For instance, in the case of system threatening circumstances, the end user may have to accept even radical changes to the contract.

The Danish Supreme Court decision *UfR 2006 1189 H* provides an illustrative example of this. This decision concerned a dispute between the non-profit private organization Dansk Internet Forum (DIFO), which was entrusted the administration of the internet domain '.dk', and a private company (DMS), which

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110 See e.g. § 36 of the German Energy Industry Act (*Energiewirtschaftsgesetz*) on the energy supplier's *Grundversorgungspflicht*.

111 P. MUSSAEUS, I. RAUSCH & M. MORAING (eds), *Verträge der Energiewirtschaft*, p 173.

112 With respect to its prices and conditions, the supplier of the last resort will only have to meet the criteria of § 39 and § 40 of the German Energy Industry Act (*Energiewirtschaftsgesetz*), cf. M. SCHULTE & R. SCHRÖDER, *Handbuch des Technikrechts* (Springer 2011), p 633; P. MUSSAEUS, I. RAUSCH & M. MORAING (eds), *Verträge der Energiewirtschaft*, p 173.

113 See - for a classical approach - e.g. F.M.B. REYNOLDS & G.H. TREITEL, 'Consideration for the Modification of Contracts', 7. *MLR (Malaya Law Review)* 1965(1), pp 1-23.

was registrant of the domain name ‘co.dk’. After the registration of the domain name ‘co.dk’, DIFO adopted new terms and conditions for the use of domain names registered under the internet domain ‘.dk’, which included a right to withdraw a registered domain name in the public interest, in certain situations against a fair compensation. Since the use of the domain name ‘co.dk’ had created some confusion for users of the domain name system, DIFO announced its intention to withdraw the domain name ‘co.dk’ and offered DMS a compensation of 25,000 DKK (approximately 6,500 EUR). Since DMS had never agreed to these new terms and conditions, and the right to withdraw a domain name was not supported by statutory law, DMS made a claim for damages. The Danish Supreme Court stated that there was a contractual relationship between DIFO and DMS, which had the character of a ‘mass contract’ (i.e. a standard contract entered into with a high number of customers), and that DIFO was entitled to make changes to this ‘mass contract’ if ‘warranted by special circumstances’.

Furthermore, terms for the supply of e.g. energy to end users often contain explicit variation clauses. From a purely commercial perspective, such variation rights often stand out as very wide.

A clause in the standard terms of the Danish electricity supply company Blue Energy provides an illustrative example: ‘BE (Blue Energy) reserves the right to unilateral change these terms and conditions, including prices. Substantial changes to the detriment of the Customer will be implemented with notice in accordance with the existing legislation’.<sup>114</sup>

A radical lack of mutuality may make the binding effect or the validity of the clause questionable under private law.<sup>115</sup> As a minimum, such contractual discretion may be limited by implementation of concepts of good faith, fair dealing, etc.<sup>116</sup> Also in contracts for the supply of universal services, certain limitations to the energy supplier’s use of the variation right will be found to exist. The above-mentioned principles of transparency, objectivity and non-discrimination will presumably restrain variations, either on a statutory basis,<sup>117</sup> or by interpretation.<sup>118</sup>

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114 See [www.blueenergy.dk](http://www.blueenergy.dk). Comparable clauses are contained in other standard terms for the supply to business customers, cf. e.g. [www.natur-energi.dk/media/1336/erhvervsbetingelser.pdf](http://www.natur-energi.dk/media/1336/erhvervsbetingelser.pdf); [www.jyskenergi.dk/vilkaar-og-betingelser-erhverv](http://www.jyskenergi.dk/vilkaar-og-betingelser-erhverv).

115 For the benefit of the public party comparable wide-ranging variation clauses are sometimes implemented into outsourcing contracts, e.g. in contracts on the outsourcing of social services, cf. O. HANSEN, ‘Public Law by Contract: The Reluctant Creation of Private Markets for Welfare Service’, 25. *ERPL (European Review on Private Law)* 2017, pp 644 et seq.

116 See e.g. the UK Court of Appeals decision 22 February 2008 in *Socimer International Bank Limited (in liquidation) v. Standard Bank London Ltd*, [2008] EWCA Civ 116 and the Supreme Courts decision 18 March 2015 in *Braganza v. BP Shipping Ltd* [2015] UKSC 17.

117 See above and e.g. Art. 3, subs. 1 of the Dir. 2009/72; § 6d of the Danish Electricity Supply Act (*lov om elforsyning*). According to Danish law, these principles specifically apply to the price setting cf. § 73 of the Danish Electricity Supply Act (*lov om elforsyning*).

However, it may prove difficult to make use of such public law standards in market settings, e.g. when assessing the size of the commercial manoeuvring room left for the supply company. Principles of objective reason and non-discrimination originate from public (administrative) law, where they restrict public authorities' use of power. Just as the obligation to contract, they contradict fundamental principles of private law. Thus, as a clear point of departure, once conferred with a contractual right, a party to a contract may use this right at will. In Scandinavian legal theory, some authors earlier argued for a possible development of a general principle of equality as embedded in contract law itself. Building primarily on fundamental rights and social rights principles of non-discrimination, *Thomas Wilhelmsson* in an article from 2000 stated the following:

A principle of equality ( ... ) could be expressed as follows. Undertakings, public authorities and other similar institutions are obliged to treat their customers equally. This means that everyone should be entitled to contract with that undertaking on the same terms and conditions as other customers, unless there are sound reasons for special treatment.<sup>119</sup>

However, *Wilhelmsson* was aware of the contradictory nature of such theorem. He acknowledged that it would require 'another attitude to the main rules and exceptions than that which has previously been expressed'.<sup>120</sup> Indeed, private law lends no or only little support for the assessment of what is to be considered as being 'objective' or deserving 'equal treatment' in a commercial contract setting.<sup>121</sup> Individual bargains are the *raison d'être* of markets.

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118 In the above-mentioned case Danish Supreme Court 23 January 2006, UfR 2006 1189 H, the Danish Supreme Court stated that when making use of its right to impose unilateral variations on its customers, DIFO was obliged 'not to discriminate its customers or to rely on non-objective criteria'.

119 T. WILHELMSSON, 40. *SSL* 2000, p 164. See also F. NYBERG, *Avtalsfrihet*, pp 79, 230.

120 T. WILHELMSSON, 40. *SSL* 2000, p 164.

121 Private law may fragmentarily or in its periphery point at principles that can help to determine the content of such doctrines. In purely commercial contractual settings, principles of non-discrimination and objective reason may be included in contracts of a certain network character, such as e.g. franchise contracts. In some legal systems legislation on franchise contracts contain a protection of the franchisee against discrimination, cf. e.g. § 23-2-2.7-2(5) of the Indiana Deceptive Franchise Practices Act (IDFPA). Within the EU there is no general regulation on the subject. A study report from 2017 from the Directorate-General for internal policies point at that the protection of franchisees within the EU may be inadequate, see [europarl.europa.eu/RegData/etudes/STUD/2016/595340/IPOL\\_STU\(2016\)595340\\_EN.pdf](http://europarl.europa.eu/RegData/etudes/STUD/2016/595340/IPOL_STU(2016)595340_EN.pdf). Where a duty of non-discrimination does not stem from the legislation, it is uncertain whether such principles (without clear support in the contract terms), can considered to be implied by interpretation as a duty of loyalty, good faith or the like, cf. e.g. A. TERRY & C. DI LERNIA, 'Franchising and the Quest for the Holy Grail: Good Faith or Good Intentions', 33. *MULR (Melbourne University Law Review)* 2009, pp 542-578. In Nordic law, it seems fair to assume that the long term and often complex nature of the franchise agreement impose upon the parties an extended duty of good faith and loyalty, cf. P. SUND-NORRCÅRD, *Tolkningen av franchiseavtal* (Juridiska fakulteten vid Helsingfors universitet 2014),

A decision from the Danish Energy Complaint Board (*Energiklagenævnet*) illustrates the difficulties (case 2007-21-458): According to the business conditions of a district heating station (HK) a discount was given to customers on the basis of registered building sizes. According to these criteria, one end user (DJ) did not qualify for the discount. However, due to its special activities (the running of laboratories and hothouses), DJ purchased a substantial amount of heating and therefore claimed that the discount practices of HK were unfair. HK argued that a yearly payment of 50,000 DKK from HK to DJ constituted a discount equivalent to DJ's status as a primary customer, whereas DJ held that this payment was a fee for HK's renting of local pre heating installations owned by DJ. The Energy Complaint Board found that the discount given to customers based on registered building sizes was 'discriminating' towards HK's other customers. However, with respect to the question of the yearly payment of 50,000 DKK, the complaint board held as follows: 'The Energy Authority finds that the payment of 50,000 DKK from (HK) to (DJ) possibly can be in conflict with the rules of the Heating Supply Act on the allowance of discounts. However, the Authority consider the contractual relation to be of such unclear nature that further submission of evidence will be necessary to clarify the dispute. Such submission of evidence can only take place within the ordinary court system. Thus, the Authority does not find a reason to pursue further and refer the question to the ordinary courts'.<sup>122</sup>

Within the contractual relationship between the supplier and the end user, the public interest may affect the *remedies for breach* at the disposal of the end user as well. In connection with the wide-ranging variation clauses that enable continuous adjustments of prices and terms, supply companies often include extensive hardship clauses and disclaimers of liability in their standard supply terms. The wording of such clauses may cause doubt as to whether the end user has any (efficient) remedy in case of the supplier's non-compliance.<sup>123</sup> Taking into

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pp 111 ff. And it is also fair to assume that franchisees may be protected under § 36 of the Danish (and common Nordic) Contracts Act (*aftaleloven*) against the use of unfair contract terms and unfair conduct. However, there is currently no legal sources that shed light on how to use standards of non-discrimination in this context. The possible horizontal effect of fundamental rights continuously leads to the consideration of the effect of anti discrimination doctrines on private law, cf. e.g. S. JANSEN & S. SOMERS, 'The Principle of Equality as a Catalyst: The Increasing Influence of the Principle of Equality on the Belgian Law of Obligations', in A. Keirse & M. Loos (eds), *Waves in Contract and Liability Law in Three Decades of Ius Commune* (Intersentia 2017), pp 61-104. See also e.g. P. ROTT, 'Dynamische und personalisierte Preise zwischen Vertragsfreiheit und Willkür', in J. Lamla, T. Hess, C. Ochs & M. Friedewald (eds), *Die Zukunft der Datenökonomie* (Springer 2019 - in press) pp 285-305. With a view point from administrative law one can note a current development in Nordic legal theory with respect to the interaction between administrative acts and contract, c.f. e.g. R. Grønved Nielsen, 2/163-188. TfR (Tidsskrift for Rettsvitenskap, 2019.

<sup>122</sup> Unofficial translation of the authors.

<sup>123</sup> As an example, the standard supply terms of Blue Energy (mentioned above) contain the following liability disclaimer: 'BE is ( ... ) without liability for customers' loss of service, loss of profit or other

consideration the generic nature of the performance, it is striking that the supplier of electricity is in a position to disclaim its liability even for the amount and the quality of the performance under the contract. Formerly, such disclaimers may have been a result of the supplier's position as a monopolist. However, in the liberalized - but intensely controlled - energy market it is fair to assume that the use of disclaimers of liability for core performances derives from the core public interests in the supply of universal services. Thus, the contractual basis for remedies for breach may be weakened by that initial lack of consent, which characterizes a substantial part of transactions in the market for supply of universal services. In case of unlawful denial of contract, the legal effect of the obligation to contract may not be clear. The rejected end user may have a (statutory) right to specific performance, but it seems unclear, whether a claim for damages can be based upon the (not existing) contract or e.g. (in addition or alternatively) on the fundamental principles of tort law.

### **3.4. *Dispute Resolution: Arbitration***

Universal services contracts with commercial end users may include binding arbitration agreements, which submit disputes concerning the provision of universal services to arbitration.<sup>124</sup> Such arbitration will be consensual in nature.<sup>125</sup> It will also be subject to comprehensive state regulation. Thus, most modern states have adopted a statutory legal framework for arbitration based on the UNCITRAL Model Law on International Commercial Arbitration (1985, amended in 2006).<sup>126</sup> In several jurisdictions, this framework also generally applies to commercial arbitration that is not international in character.<sup>127</sup> We will therefore use the Model Law as basis for our analysis.

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indirect losses, unless BE has acted intentionally or grossly negligent. BE is never liable for damage or loss due to faults or interruptions in the power grid, nor to the technical quality of the supplier including voltage level, frequency, and noise conditions. BE is furthermore not liable for any limitations or restrictions imposed by the electricity grid company, the system operator, or the Nordic electricity market exchange, Nord Pool'. (unofficial translation of the authors). Comparable clauses are contained in other B2B standard terms, see e.g. [natur-energi.dk/media/1336/erhvervsbetingelser.pdf](http://natur-energi.dk/media/1336/erhvervsbetingelser.pdf).

124 Arbitration agreements with consumers concerning future disputes may not be binding or may be otherwise unenforceable in many jurisdictions, see e.g. G. BORN, *International Commercial Arbitration* (Kluwer Law International, 2nd edn 2014), pp 1014-1027. Examples of Danish suppliers using such arbitration agreements in their standard commercial terms are [www.jyskeenergi.dk](http://www.jyskeenergi.dk) and [www.gasel.dk](http://www.gasel.dk).

125 For an analysis of the consensual nature of arbitration, see, in particular, A.M. STEINGRUBER, *Consent in International Arbitration* (Oxford: Oxford University Press 2012).

126 Arbitration is also subject to important international conventions, including the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards (1958).

127 See G. BORN, *International Commercial Arbitration*, pp 127-128.

In a private governance perspective, the Model Law implies a delegation of state power to private actors (arbitrators) to adjudicate disputes with a legally binding and enforceable effect as long as the private arbitration adheres to fundamental ‘procedural justice values’, the dispute is capable of settlement by arbitration, and the arbitral award is not contrary to public policy.<sup>128</sup> The Model Law defines important rights and duties of arbitrators, some of which are mandatory, and to some extent, it also regulates the remedies available for breach of these duties. However, the Model Law provides no exhaustive regulation of these matters. Instead, it empowers the arbitral tribunal to decide on all matters concerning the conduct of arbitral proceedings to which the parties do not agree.<sup>129</sup> In exercising this discretion, arbitrators must of course adhere to the fundamental principles laid down in the Model Law, including the principle on equal treatment of the parties.<sup>130</sup>

Disputes arising from universal services contracts can involve public values and matters of public interest such as violations of the general requirement for ‘fair, objective and non-discriminating’ price calculation principles.<sup>131</sup> Despite this public interest, such disputes are capable of settlement by arbitration in many (if not all) jurisdictions.<sup>132</sup> Thus, state courts may set aside the award and/or refuse recognition and enforcement of the award only if the arbitral award is in conflict with the public policy of the state.<sup>133</sup> Public policy (*ordre public*) is generally a vague concept and many jurisdictions perceive it as a (very) narrow concept.<sup>134</sup> State courts can only set aside an arbitral award if a party starts timely proceedings to this end, which none of the parties may have an incentive to do (e.g. when a discrimination only harms third parties).<sup>135</sup> A party may seek recognition and enforcement of the award in foreign jurisdictions, where the award does not violate public policy. Consequently, the power of state courts to set aside arbitral awards or to refuse recognition and enforcement of awards only provide limited safeguards of public values and interests in disputes submitted to arbitration.

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128 Articles 34–36 of the UNICTRAL Model Law on International Commercial Arbitration and the New York Convention often constitute the basis for such state regulation. As mentioned above, arbitration also presupposes a valid arbitration agreement.

129 Article 19(2) of the Model Law.

130 See, in particular, Art. 18 of the Model Law.

131 See *supra* s. 3.3.

132 In recent decades, the general trend in many jurisdictions has been an expansion of disputes capable of settlement by arbitration, including disputes involving elements of a (strong) public interest. For an overview, see e.g. G. BORN, *International Commercial Arbitration*, Ch. 6.

133 See Arts 34 and 36 of the Model Law.

134 See, in particular, the comparative analysis in F. GODHOOSI, *International Dispute Resolution and the Public Policy Exception* (Routledge 2016), who identifies four different approaches (paradigms) concerning public policy: (1) Social and economic life (public sphere), (2) basic notions of morality and justice, (3) fundamental principles of law and (4) international public policy.

135 See Arts 34 and 36 of the Model Law.

This makes it pertinent to consider whether arbitrators have a duty to safeguard public values and interests relevant for the dispute submitted to arbitration (such as the non-discrimination principle mentioned in ss 3.2 and 3.3). If a party raises the issue of discrimination in an arbitration, arbitrators will normally have an obligation to apply any applicable non-discrimination principle.<sup>136</sup> If none of the parties raises the issue, e.g. because the discrimination only harms third parties, it is less clear whether arbitrators may or must apply any applicable non-discrimination principle. In principle, arbitrators could have a duty to *ex officio* investigate the issue (e.g. if information in the case suggests that the non-discrimination principle might be infringed), to give judicial ‘hints and feedback’ to the parties concerning the issue and (eventually) to apply the non-discrimination principle even though it was not raised by the parties.<sup>137</sup> The basis for establishing such *ex officio* obligations of arbitrators is, however, generally limited.<sup>138</sup>

Even if arbitrators have duties to safeguard public values and interests, the remedies for breach of the duties are uncertain. A party may raise a claim for the setting aside or refusal of recognition and enforcement of the award, but (again) this will depend, in particular, on the concept of public policy which, as mentioned, is (very) narrow in many jurisdictions. In some jurisdictions, the arbitrator might also incur a liability in damages towards the parties. However, a party may not have an incentive to make use of such remedies (e.g. if the discrimination has only harmed third parties), and it seems impossible to provide any remedies to third parties (including representatives for diffuse and collective/public interests) without clear statutory support. In sum, arbitration law has limited capability to ensure the safeguarding of public values and interests in disputes submitted to arbitration such as the above-mentioned non-discrimination principle.

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136 See Art. 28 of the Model Law and e.g. F. FERRARI & G. CORDERO-MOSS (eds), *Iura Novit Curia in International Arbitration* (JurisNet 2018).

137 State court judges may have such obligations in civil litigation, see e.g. A.S. HARTKAMP, ‘Ex Officio Application in Case of Unenforceable Contracts or Contract Clauses - EU Law and National Laws Confronted’, in L. Gullifer & S. Vogenauer, *English and European Perspectives on Contract and Commercial Law: Essays in Honour of Hugh Beale* (Hart Publishing 2017), pp 467-484. On the *ex officio* obligations developed by the CJEU under EU law, see e.g. K. LENAERTS, I. MASELIS & K. GUTMAN, *EU Procedural Law* (Oxford: Oxford University Press 2014), pp 131-136.

138 The Model Law does not explicitly impose such obligations on arbitrators. Nevertheless, commentators argue that arbitrators have an implicit duty (to take reasonable measures) to render a binding and enforceable arbitral award, see e.g. G. BORN, *International Commercial Arbitration*, p 1393. Arguably, arbitrators should therefore also have a duty to *ex officio* take into consideration any matters which may lead to the setting aside or refusal of recognition and enforcement of the award, including matters that would bring the award in conflict with the public policy of the state. However, since the concept of public policy is (very) narrow in many jurisdictions, the duty of arbitrators will in this regard be equally limited.

On a more general level, it seems that arbitration as a means of dispute resolution creates challenges in private law that are similar to those identified *supra* 3.2. and 3.3. As mentioned, the Model Law leaves significant discretion to arbitrators to decide when the parties disagree with regard to matters concerning the conduct of the arbitral proceedings, including the duties of the arbitrators. In principle, this leaves room for private law to govern the exercise of this discretion within the framework established by the Model Law. It is in this context that challenges in private law seem to emerge.

First, the normative basis in private law for governing arbitration is unclear. Several potential legal sources are available: Contract law (such as the obligation to act in good faith and principles of agency law), civil procedure law (based on the status of arbitrators performing a judicial role similar to judges in public courts) or a *sui generis* arbitration law. In international commercial arbitration, even more potential sources are available: The contract law, civil procedure law or *sui generis* arbitration law of a particular jurisdiction (typically the law of the seat of the arbitral tribunal) or a non-national law based on international standards for international commercial arbitration ('arbitral common law'). These many potential legal sources have resulted in different legal theories about the 'legal nature of arbitration'.

The theories emphasize either the contractual nature of arbitration (contractual theory), the judicial (public) nature of arbitration as originating from a delegation from one or more state legal orders (judicial or jurisdictional theory), a mix of both (hybrid theory) or the autonomous nature of arbitration (autonomous theory).<sup>139</sup> Such theories offer different perspectives on the legal effects of arbitration, including the extent to which private law governs arbitration and, if so, whether this is the private law of a particular jurisdiction (typically the law of the seat of the arbitral tribunal) or an autonomous (non-national) private law (delocalization theory).<sup>140</sup> Other theories emphasize that arbitrators are agents of a greater (transnational) arbitration community, which builds arbitral institutions and thus the capacity to govern.<sup>141</sup> This *judicialization* of arbitration may

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139 See, in particular, A. SAMUEL, *Jurisdictional Problems in International Commercial Arbitration: A Study of Belgian, Dutch, English, French, Swedish, Swiss, U.S. and West German Law* (Zürich: Schulthess Polygraphischer Verlag 1989); A.W. ROVINE (ed), *Contemporary Issues in International Arbitration and Mediation: The Fordham Papers* (Brill Nijhoff, vol. 4 2010); J. PAULSSON, *The Idea of Arbitration* (Oxford: Oxford University Press 2013); E. GAILLARD, *Legal Theory of International Arbitration* (Brill Nijhoff 2014); G. BORN, *International Commercial Arbitration*, pp 214-217.

140 For an overview of the theoretical discussions about 'delocalization' of arbitration, see e.g. G. CORDERO-MOSS, *International Commercial Arbitration: Party Autonomy and Mandatory Rules* (Tano Aschehoug 1999), pp 180-196.

141 See A.S. SWEET & F. GRISEL, 'The Evolution of International Arbitration: Delegation, Judicialization, Governance', in W. Mattli & T. Dietz (eds), *International Arbitration and Global Governance: Contending Theories and Evidence* (Oxford: Oxford University Press 2014), who

eventually lead to a *constitutionalization* by embedding arbitral legal orders within an overarching legal framework that includes general principles of law, international economic law, and human rights, including property rights and guarantees of due process.<sup>142</sup>

Neither the Model Law nor the above-mentioned theories have resulted in a common and clear understanding of the law governing arbitration beyond agreements between the parties and statutory arbitration laws. In these respects, the private law that governs arbitration – and, in particular, international commercial arbitration – suffers from a significant *loss of orientation*. This has implications, *inter alia*, for establishing the arbitrators' duties.<sup>143</sup>

Challenges in private law also emerge when we look at *remedies for breach* of arbitrators' duties. From a private law perspective, the Model Law rules on setting aside, recognition and enforcement of arbitral awards will generally rule out a claim for specific performance of any duty of arbitrators beyond the statutory duties of arbitrators.<sup>144</sup> In addition, statutory law in several jurisdictions exempt arbitrators from liability in the performance of their core duties as arbitrators.<sup>145</sup> Thus, the two most important private law remedies for breach of arbitrators' duties – specific performance and liability – are subject to very significant restrictions.

### 3.5. Conclusions

#### 3.5.1. Cross-Observations

State regulation of the sectors for supply of universal services leaves very little room for party autonomy. However, contracts play a major role as a legal basis for the implementation of public values. Thus, without understanding the complex interplay between the 'column 1' of statutory regulation and the implementation of contractual practices in 'column 2', the legal implications of private governance of universal services cannot be properly assessed. Generally, a duty to supply placed upon private universal service providers will also mean an obligation to contract with anyone demanding the service on terms and conditions compliant to the aim and purpose of the sector legislation. The obligation to contract may emerge

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identify three different models for arbitration: The contractual model, the judicial model and the constitutional model.

142 *Ibid.*

143 See e.g. G. BORN, *International Commercial Arbitration*, p 1985, 'Given the essential importance of the arbitrators' obligations to the arbitral process, there is a remarkable lack of authority concerning even the general nature of these obligations ... '.

144 See Arts 34 and 36 of the Model Law.

145 See e.g. s. 29(1) of the UK Arbitration Act 1996, 'An arbitrator is not liable for anything done or omitted in the discharge or purported discharge of his functions as arbitrator unless the act or omission is shown to have been in bad faith'. More generally, see G. BORN, *International Commercial Arbitration*, pp 2027 et seq.

expressly from the legislation, but it might also be a consequence of duties placed on the private suppliers to implement principles of non-discrimination.

Despite the extensive regulation and the implementation of public values into private markets for universal services, private supply companies and business-consumers are free to opt-out of the ordinary court system as forum for dispute resolution. The use of private and usually confidential arbitration procedures seems to contradict the apparent political request for public control since the parties to the contract may have no incentive to pursue public goals, nor will arbitrators have the same obligations to pursue public interests as judges in the ordinary court system. Thus, neither the impact on private law of regulation nor of implementation of public values in the sectors for universal services can be assessed without considerable emphasis on the chosen means of dispute resolution ('column 3').

### 3.5.2. *State-Driven Private Governance: An Amputated Private Law*

The analysis shows that regulatory adjustments made in private law with the aim to control the activity in the liberalized markets for universal services are significant. The mandatory elements of contract formation contradicts private law's fundamental principle of party autonomy and creates a conflict of values that persists down the line of private law's systematics and reasoning, from the formation to completion of contracts. The inverted point of departure leads to a legitimacy dilemma and loss of orientation in contract law, now placed between the conflicting poles of legality and autonomy.

As shown, on the one hand the obligation to contract challenges fundamental principles of mutuality, by justifying unilateral variation rights. On the other hand, public law doctrines of e.g. transparency, objectivity and non-discrimination (which are closely connected to the obligation to contract) limit the free choice of the private supply company. This public law impact on contract law suggests a pull away from contract as the governing legal instrument in the direction of public ordering or administrative acts, often embedded with these exact characteristics. Without a clear hierarchy between private and public law's founding norms and principles, the legal position of the parties hereby becomes (highly) uncertain.

Public law's influence on private law further seems to affect remedies, e.g. the private supply company's liability for breach of contract. Possibly, due to the same public values and interests that justify the supply duty, the supplier will generally be subject to a very limited liability regime, exempting liability for any damage caused by non-performance. The complexity of the distribution system and the public tasks placed upon the private supply companies may possibly be considered as justification for such limitations and disclaimers. However, the potential of private law to govern the supply of universal services in private markets relies on the available remedies for breach. What is a contract without remedies in case of breach?

On this background, the use of arbitration is striking. The nature of the (contractual) relationship between the contracting parties and the arbitrator is unclear, bearing itself many of the characteristics of state driven private governance. States do seem more reluctant with respect to regulation of private arbitration and more confident in leaving room for party autonomy than in the example of the provision of universal services, but private law's ability to support the fundamental public values at stake in arbitration is still doubtful. This is all the more so since the private nature and confidentiality of arbitration clearly contradicts the public demand for transparency and can be assumed to bar any aggrieved party from knowledge of and evidence of e.g. discriminating business conduct.

#### **4. Concluding Remarks: Two Main Findings: And Further Questions**

The analysis above has led to two main findings. They both lead to more questions.

*Firstly*, the study seems to indicate that a thorough private law analysis of a private governance phenomenon may require looking at the three functionalities of the governance system as a whole. For example, it is not possible to examine the possible liability of a supply chain certifier (column 2) *vis-à-vis* third parties unless the possible liability of the chain leader (column 1) is also examined. Likewise, an examination of the contract law related to contracts for the supply of energy services (column 2) requires an understanding of the regulatory framework behind the privatization of these services (column 1) as well as an understanding of the extent to which the public values embedded in the contracts can be presumed to be protected in the chosen dispute resolution system (column 3). More examples can be found in sections 2 and 3 above. Moreover, such a cross column analysis may also reveal some stunning internal contradictions in the governance system. As an example could be mentioned the pursuance of transparency goals in the regulatory framework for the provision of universal services combined with the use of private arbitration as a dispute resolution mechanism which does not generally require any form of publicity. Also the widespread use of informal dispute resolution mechanisms such as mediation in conflicts concerning CSR can be seen as contradicting the fact that the soft law CSR standards are increasingly being 'hardened' by incorporation into contracts. Such contradictions may weaken the potential of private law as a private governance tool (see further below).

*Secondly*, the examples seem to indicate that private law is rich on mechanisms that can be activated in a private governance setting. Contract is an obvious governance instrument because of its ability to steer and serve a regulatory function but also tort law can have important functions both with regard to developing standards and serving as an accountability mechanism. In addition, both contract law and tort law are today viewed as flexible tools in their sphere of command. However, when it comes to serving as a tool for private actors' pursuance of public interests and values in today's private governance systems, private law is also challenged. Moreover, the challenge seems to have a different character in the

two chosen examples. In the supply chain example, private law is pushed to its limits. The phenomenon of private governance seems to call for the use of what could be called an ‘exception-based’ private law. This picture is clear in contract law but can to some extent also be found in tort law. Relying on an ‘exception-based’ private law also implies relying on principles that are not always fully developed or that are ‘invented’ in the concrete case, giving rise to uncertainty for all actors in the governance system and for third parties that are external to the governance system. Based on this observation, one might have assumed that state driven private governance would give rise to less uncertainty since the private law effects could be clearly regulated in the public law framework surrounding the governance system. However, as the example of universal services shows, this seems not to be the case. To the contrary, in these cases, private governance seems to have an even more disturbing effect on private law. In the example of universal services, the ‘invasion’ of public law principles, stemming from statutory frameworks, into private law has as a consequence that basic private law principles – such as freedom of contract – disappear from the private law system. This ‘amputation’ causes a considerable loss of orientation in the private law system where public law principles such as legality and equality come to compete with private law notions of autonomy and mutuality. Very often the outcome of this rivalry is almost unpredictable.

In our analysis, we have used the supply chain as an example of a market driven governance system and the supply of universal services as an example of a state driven private governance system. The analysis raises the question whether the observed differences in the way private law is affected in these two categories would also be recognizable in other examples of market driven and state driven private governance systems. For example, it might be assumed that the same pattern would appear in an analysis of market driven platform law systems and state driven contracting out systems, although, as observed above, state driven systems may come in different versions with varying regulatory intensity. The analysis also raises the question whether the distinction between market driven and state driven private governance systems would be relevant in other respects. For instance, it must be assumed that the involvement of the state as a ‘delegator’ of tasks to private actors will affect the basic risk- and liability distribution both in contract and tort in any state driven private governance system. Thus, state actors will in some respects be regarded as being better capable of absorbing risks than private actors. In other respects, however, state actors may be protected by a special immunity or lenient liability rules. Such factors may influence also the amount of risk and liability allocated to the private party in the private governance system.

*In general*, the analysis may be seen as indicating a largely unexplored potential of private law to function as a tool in private governance systems. At the same time, the challenges posed to private law by the phenomenon of private governance may call for further development of basic private law concepts. Thus, an ‘exception based’ and ‘amputated’ private law hardly constitutes a viable frame

for accommodating the widespread phenomenon of private governance. It is a fundamental challenge in this regard that the often used alternative dispute resolution mechanisms, such as mediation and arbitration, are focused on solving individual conflicts rather than creating transparent precedence. Thus, the development of a coherent new private law, adapted to its new public role, may be dependent on a parallel development of the role and nature of private dispute resolution mechanisms. If such development in private law does not take place, instead of giving rise to new synergies in the cross field between state and market, private governance may risk expanding into a hazy gap between public and private law. Here, both societies and markets will suffer from a lack of fundamental principles of legal protection.

