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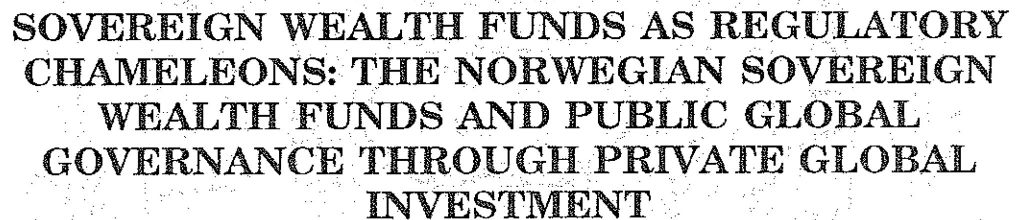

# SOVEREIGN WEALTH FUNDS AS REGULATORY CHAMELEONS: THE NORWEGIAN SOVEREIGN WEALTH FUNDS AND PUBLIC GLOBAL GOVERNANCE THROUGH PRIVATE GLOBAL INVESTMENT

LARRY CATÁ BACKER

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LARRY CATÁ BACKER*


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## I. INTRODUCTION

For much of the end of the last century, legislatures and courts have

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been grappling with the problems of state participation in private markets[1] and private market actors participating in governance activities within and between states.[2] These issues have become acute in the first decade of the twenty-first century as a number of forces intersect—an increasing willingness of states to invest their wealth abroad in instruments other than the debt securities of other nations, the rise of transnational normative frameworks for global market and business behavior, the development of a severe economic collapse in the last years of the decade, and an increasing understanding of the public role of private actors, especially in places where state authority is weak. Among the more visible manifestations of these tectonic changes in the way in which the global order is organized are sovereign wealth funds.[3] Over the last decade they have been transformed from a simple and relatively benign sovereign vehicle for the investment of excess wealth in a discrete way,[4] to an important force in global finance.[5] According

1. The European Union has been the most thoughtfully engaged in this issue. *See, e.g.*, Larry Catá Backer, *The Private Law of Public Law: Public Authorities as Shareholders, Golden Shares, Sovereign Wealth Funds, and the Public Law Element in Private Choice of Law*, 82 TUL. L. REV. 1801 (2008) [hereinafter Backer, *Private Law of Public Law*] (considering this issue from a conflicts perspective).

2. *See, e.g.*, Larry Catá Backer, *Multinational Corporations as Objects and Sources of Transnational Regulation*, 14 ILSA J. OF INT'L & COMP. L. 499, 508-517 (2008) [hereinafter Backer, *Objects and Sources*]; *see generally*, Larry Catá Backer, *Multinational Corporations, Transnational Law: The United Nation's Norms on the Responsibilities of Transnational Corporations as a Harbinger of Corporate Social Responsibility in International Law*, 37 COLUM. HUM. RTS. L. REV. 287 (2006) [hereinafter Backer, *United Nation's Norms*].

3. We start with a simple definition, one proposed by Clay Lowery, Undersecretary for International Affairs in the second Bush administration: "a government investment vehicle which is funded by foreign exchange assets, and which manages these assets separately from official reserves." Stephen Jen, *Currencies: The Definition of a Sovereign Wealth Fund*, Morgan Stanley, Global Economic Forum at 2 (Oct. 25, 2007), http://sovereignwealthfunds.files.wordpress.com/2008/01/the-definition-of-a-sovereign-wealth-fund-morgan-stanley-october-2007.pdf (quoting Undersecretary Lowery). Mr. Jen suggests a more market participatory, though slightly wary, definition: "a SWF needs to have five ingredients: 1. Sovereign; 2. High foreign currency exposure; 3. No explicit liabilities; 4. High risk tolerance; 5. Long investment horizon." *Id.* He would distinguish among sovereign wealth funds, sovereign pension funds and reserves. *See id. See* discussion *infra* Section II discussing the difficulties of definition and its regulatory consequences.

4. "In 1953, eight years before its independence from the United Kingdom, Kuwait established the Kuwait Investment Board to invest its surplus oil revenue. That was perhaps the first ever 'sovereign wealth fund' (SWF), although the term would not exist for another 50 years." Robert M. Kimmitt, *Public Footprints in Private Markets: Sovereign Wealth Funds and the World Economy*, 87(1) FOREIGN AFFAIRS 119 (2008). Sovereign wealth funds are typically the result of national budget surpluses, often accumulated over the years due to favorable macroeconomic, trade and fiscal positions, coupled with long-term budget planning and spending restraint. Usually, these funds are set up with one or more of the following objectives: "insulate the budget and economy from

to Congressional Research Service, such SWFs currently manage between $1.9 and $2.9 trillion, and they are expected to grow to over $12 trillion by 2015.[6] Similarly, the International Monetary Fund indicates that the expected growth of SWFs' assets will be over $10 trillion in the next 5 to 10 years.[7] And thus an irony, though they are creatures of states, they also tend to challenge state power to order its internal relations, and the legal systems under which these arrangements are maintained.

At the international level there have been public and private efforts to create either voluntary codes of behavior for such funds, including collective efforts backed by states with important sovereign wealth funds.[8] These tend to privilege transparency, disclosure and equivalent treatment with private funds similarly operated.[9] On the other hand, host states have been tending toward a jurisprudential position that significantly narrows the circumstances under which a state ought to be

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excess volatility in revenues, help monetary authorities sterilise unwanted liquidity, build up savings for future generations, or use the money for economic and social development." *See* Andrew Rozanov, *Who holds the wealth of nations?*, STATE STREET GLOBAL ADVISORS at 1 (August 2005), *available at* http://www.libertyparkusafd.org/lp/Hancock/Special%20Reports/Sovereign%20Wealth%20Funds/Who%20Owns%20the%20Wealth%20of%20Nations%20-%202005.pdf.

5. *See* Gerard Lyons, *State Capitalism: The Rise of Sovereign Wealth Funds*, 14 LAW & BUS. REV. AM. 179, 202-238 (2008) (providing data on the largest funds). As the organizers of the Georgetown Journal of Internal Law 2009 Conference astutely described it,

> Controlling vast pools of capital and investing globally, sovereign wealth funds often operate without full regulatory supervision and with objectives other than maximizing return on investment. These powerful funds raise legal, economic, and strategic security issues that private investors do not. As the number and size of sovereign funds continue to grow, the global legal community is confronted by novel issues of both public and private international law.

Featured Symposia, *2009 Symposium*, GEO. J. INT'L L. (2009), *available at* http://www.law.georgetown.edu/journals/gjil/symposia.html (last visited Nov. 21, 2009).

6. Martin A. Weiss, Cong. Research Serv., *Sovereign Wealth Funds: Background and Policy Issues for Congress*, at 1 (Sept. 3, 2008), http://opencrs.com/document/RL34336.

7. Delia Velculescu, Norway's Oil Fund Shows the Way for Wealth Funds, IMF SURVEY MAGAZINE, July 9, 2008, http://www.imf.org/external/pubs/ft/survey/so/2008/POL070908A.htm.

8. *See generally*, International Working Group of Sovereign Wealth Funds, Sovereign Wealth Funds: Generally Accepted Principles and Practices 1-2 (October 2008), http://www.iwg-swf.org/pubs/eng/santiagoprinciples.pdf [hereinafter *Santiago Principles*].

9. *See infra* notes 19, 91-92, 95-99, 104-105, 120-121, 310-311 and accompanying text. *See also* Gordon L. Clark & Roger Urwin, *Best-Practice Pension Fund Governance*, 9 J. OF ASSET MANAGEMENT 2 (2008).

treated like a private entity, at least for purposes of applying the obligations the European Union's treaty framework.[10] The United States, in contrast, has tended to avoid direct regulation.[11] Sovereign wealth funds can fall within a variety of regulatory fields depending, for example, on the object of investment,[12] the form of investment,[13] and the relation to sovereign activity.[14] Essentially, however, sovereign wealth funds in the United States are treated as sovereign for tax

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10. This evolution is discussed in Backer, *Private Law of Public Law*, *supra* note 1, at 1833-45. *See also* Peer Zumbansen, *The ECJ, Volkswagon and European Corporate Law: Reshaping the European Varieties of Capitalism*, 8 GERMAN L.J. 1027 (2007); Johannes Adolff, *Turn of the Tide?: The "Golden Share" Judgments of the European Court of Justice and the Liberalization of the European Capital Markets*, 3 GERMAN L.J. (2002), *available at* http://www.germanlawjournal.com/index.php?pageID=11&artID=170.

11. This approach is discussed in Larry Catá Backer, *Sovereign Wealth Funds and Regulatory Responses to the Financial Markets Crisis*, 19 TRANSNAT'L L. & CONTEMP. PROBS. (forthcoming 2009) [hereinafter Backer, *Regulatory Responses*].

12. Thus, for example, sovereign wealth funds can be treated like other foreign investors in connection with investment activities that touch on national security concerns. In that regard, the American Committee on Foreign Investment in the United States was established by executive order in 1975 to review inbound foreign investments. *See* Exec. Order No. 11858(1)(b), 40 Fed. Reg. 20263 (May 7, 1975). This regulatory system was strengthened in 2007 but remains otherwise unchanged. *See* Mark E. Plotkin, *Foreign Direct Investment by Sovereign Wealth Funds: Using the Market and the Committee on Foreign Investment in the United States Together to Make the United States More Secure*, 118 YALE L.J. Pocket Part 88 (2008). In addition, the President has the authority to block a foreign acquisition under the Defense Production Act (commonly known as the Exon-Florio provision) where there is a credible threat to national security and no other recourse at law. *See* Defense Production Act § 721(a)(3), Pub. L. No. 110-49, 121 Stat. 246 (2007) (to be codified at 50 U.S.C. app. § 2170); Christopher M. Weimer, *Foreign Direct Investment and National Security Post FINSA 2007*, 87 TEX. L. REV. 663 (2009).

13. *See, e.g.*, *Sovereign Wealth Funds, Testimony Before the Comm. on Banking, Housing and Urban Affairs* (April 24, 2008), *available at* http://www.federalreserve.gov/newsevents/testimony/alvarez20080424a.htm (statement of Scott G. Alvarez, General Counsel Board of Governors of the Federal Reserve System) ("As a general matter, the same statutory and regulatory thresholds for review by the federal banking agencies apply to investments by sovereign wealth funds as apply to investments by other domestic and foreign investors in U.S. banks and bank holding companies.").

14. Thus, for example, income of foreign governments received from investments is generally treated as exempt from taxation. *See* I.R.C. § 892(a)(1) (1986). Under the Bank Holding Company Act, there is a distinction between states and the corporations through which states may operate in the banking sector. *See* Bank Holding Company Act of 1956, 12 U.S.C. §§ 1841-50 (2006); Banca Commerciale Italiana, 68 Fed. Res. Bull. 423 (1982). For discussion, see Michael Gruson, and Uwe H. Schneider, *The German Landsbanken*, 1995 COLUM. BUS. L. REV. 337, 428-30 (1995). Yet, sovereign immunity rules in the United States subjects sovereign activity in or connected with the United States to liability in U.S. courts. *See* Foreign Sovereign Immunity Act of 1976, 28 U.S.C. §§ 1330, 1332, 1391(f), 1441(d), and 1602–1611; Republic of Argentina v. Weltover, 504 U.S. 607 (1992).

purposes, and used to invest in those instruments traditionally used by sovereigns to manage their currencies and reserves.[15] Otherwise, sovereign wealth funds will be treated as private entities for purposes of immunity from suit, investment suitability as a foreigner and obligation to comply with generally applicable law.[16]

At the root of these various approaches is both fear and desire—especially among host states. As Gerard Lyons recently noted, these states have come to understand three crucial implications of sovereign wealth funds—first, that their influence is growing in all financial markets and across all financial products; second, that host and home states will clash over what SWFs can buy and where; and third, that the first two implications are powerful evidence of a great shift in the world economy, one not necessarily to the benefit of Western investment host states, now more dependent on direct foreign investment.[17] Yet that fear and desire reflects a deeper ambivalence in approach to regulation, one that touches on the complexity of the sovereign wealth fund entity and its use. From a perspective of the formalities of law and organization these entities appear to be creatures of the state that funds and controls them—a public purpose public owned entity. But from a functionalist perspective, these entities appear to behave like other private investment entities similarly constituted. They participate rather than regulate.

Yet, from this ambivalence something approaching a consensus of views has emerged on the approach to regulating sovereign wealth funds.[18] That approach is grounded on a measure of transparency, some minimum amount of institutionalization of funds and their activities, so that they exist separate from the political and administrative ministries of a state, and a strict limit on objectives of investment.[19] This consensus is nicely evidenced in the Santiago Principles.[20] The objectives are to ensure that host states do not feel threatened by these investment vehicles, and can approach their governance (and acceptability) in the same way that they approach the regulation of private

15. *See*, Edward F. Greene & Brian A. Yeager, *Sovereign Wealth Funds—A Measured Assessment*, 3(3) CAP. MKTS. L.J. 247, 248 (2008).

16. *See, e.g.*, Matthew Melone, *Should the United States Tax Sovereign Wealth Funds?*, 26 B.U. INT'L L.J. 143 (2008).

17. *See* Lyons, *supra* note 5, at 179-180. See Kimmitt, *supra* note 4, for a discussion from the perspective of a former U.S. administration official.

18. For an articulation of the premises of this consensus, see Kimmitt, *supra* note 4.

19. *See* Sovereign Wealth Fund Institute, *Linaburg-Maduell Transparency Index*, http://www.swfinstitute.org/research/transparencyindex.php (last visited Apr. 3, 2009).

20. *See Santiago Principles*, *supra* note 8, at 5, 11.

aggregations of investment capital. For that purpose, the objectives of investment take on an important role. Critical to that role is an understanding that SWFs ought to strive to adhere to a private investor model of investment. The object of SWFs should not be to project state power. Rather, it is to "maximize risk-adjusted financial returns in a manner consistent with its investment policy, and based on economic and financial grounds."[21] If investment decisions deviate from that model, those deviations ought to be disclosed,[22] suggesting that such deviation might open that fund to special regulation. SWF management "should be consistent with what is generally accepted as sound asset management principles,"[23] and it should not take "advantage of privileged information or inappropriate influence by the broader government."[24] Lastly, SWFs should exercise ownership rights "in a manner that is consistent with its investment policy and protects the financial value of its investment."[25] Effectively, if a sovereign wealth funds acts like a private investor, if it ceases to exercise its authority as a regulator rather than a participant, then it ought to be viewed as a benign instrument useful to the development of global financial markets, and regulated as such.[26]

This consensus makes two important assumptions. The first is that private funds have no regulatory effect—they do not project political power as states do, or for the same ends. The second is that it is possible to model those private behaviors and use this as a benchmark for distinguishing between benign sovereign wealth fund activities—

21. *See id.* at 8, GAPP Principle 19.

22. *See id.* at GAPP 19.1 Subprinciple.

23. *See id.* at GAPP 19.2 Subprinciple.

24. *See id.* at GAPP 20 Principle.

25. *See id.* at 9, GAPP 21 Principle. On this point, see also Paul Rose, *Sovereigns as Shareholders*, 87 N.C. L. REV. 83 (2008) (arguing that this approach works best in states with strong regulatory traditions and institutions).

26. *See* Organization for Economic Cooperation and Development [OECD], OECD Investment Committee, *Sovereign Wealth Funds and Recipient Country Policies: Report by the OECD Investment Committee*, at 6 (Apr. 4, 2008), *available at* http://www.oecd.org/dataoecd/34/9/40408735.pdf ("The resulting framework will foster mutually beneficial situations where SWFs enjoy fair treatment in the markets of recipient countries and these countries can confidently resist protectionism pressures."). This is essentially the idea expressed in any number of scholarly explorations of the problem. *See, e.g.*, Edwin M. Truman, *Sovereign Wealth Funds: Debunking Four Popular Myths* (Aug. 14, 2008), http://www.voxeu.org/index.php?q=node/1539; Steven J. Pacini, *The Effect of Sovereign Wealth Funds*, 27 REV. BANKING & FIN. L. 356 (2008). Yet, it is important to remember as well that in places like the United States, the result might in some cases be no regulation at all. *See, e.g.*, Tamar Frankel, *Private Investment Funds: Hedge Fund Regulation by Size*, 39 RUTGERS L.J. 657 (2008).

activities that ought not to be specially regulated—from political sovereign wealth fund activities that might be specially regulated. As a result, if a model of private investment activity could be understood and constructed, then there would be no reason to treat funds differently merely because one type is owned by a state and the other is not. And that, essentially, has been the thrust of discourse and activity.[27] Whether in the form of soft law or hard law at the municipal or supra-national levels, the idea is substantially stable—sovereign wealth funds that adopt the behaviors of private investment fund can be treated no worse than private funds in host states. As a consequence, special or disabling regulation is unnecessary, and these funds can contribute to the integrity of global private financial markets.[28] Thus understood, the challenge for domestic and international regulatory responses to the SWF phenomenon is, while important, conceptually manageable.[29]

Yet if these assumptions are *not* valid, then the current project of regulatory reform and its conceptions of both sovereign wealth funds and private investment funds might be misdirected at best and cause some harm at worst. Every powerful private actor affects social perceptions and behavior by their conduct and their diffusion of knowledge and outlook.[30] The U.S. has long feared the expression of public power by private entities either through interventions in private markets,[31] or in the electoral process.[32] And increasingly there is recognition that

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27. For more on this idea see the aptly titled article, Arina V. Popova, *We Don't Want to Conquer You; We Have Enough to Worry About: The Russian Sovereign Wealth Fund*, 118 YALE L.J. POCKET PART 109 (2008).

28. "SWF investments are both beneficial and critical to international markets. For that purpose, it will be important to continue to demonstrate—to home and recipient countries, and the international financial markets—that SWF arrangements are properly set up and investments are made on an economic and financial basis." *Santiago Principles*, *supra* note 8, at 4. INTERNATIONAL MONETARY FUND, SOVEREIGN WEALTH FUNDS—A WORK AGENDA (Feb. 29, 2009), *available at* http://sovereignwealthfunds.wordpress.com/2008/01/22/what-is-a-sovereign-wealth-fund-a-working-definition (last visited March 30, 2009) ("SWFs can mitigate market stress.").

29. For an example of the form this manageability takes, see, for example, Ronald L. Gilson & Curtis J. Milhaupt, *Sovereign Wealth Funds and Corporate Governance: A Minimalist Response to the New Mercantilism*, 60 STANFORD L. REV. 1345 (2008).

30. The classic focus of study has been non-governmental organizations. *See, e.g.*, Bob Reinalda, *Private in Form, Public in Purpose: NGOs in International Relations Theory*, *in* NON-STATE ACTORS IN INTERNATIONAL RELATIONS 11 (Bas Arts, Math Noortmann & Bob Reinalda, eds. 2001).

31. For the classic expression of that fear in the U.S. courts, *see* Louis K. Liggett Co. v. Comptroller of the Fla., 288 U.S. 517 (1933) (Brandeis, J., dissenting in part).

32. For the tensions in public perceptions about the extent of private entity interventions in national politics, *compare* First National Bank of Boston v. Bellotti, 435 U.S. 765 (1978) (constitutional right of corporations to participate in political activity affecting their interests), *with* Austin

policy can be as easily affected through imposition of obligations on entities as on states.[33] That has been the thrust of the efforts through the Organization for Economic Cooperation and Development (OECD)[34] to impose a soft law framework for the regulation of multinational enterprises.[35] In recent statements through its administrative bodies, it has become increasingly clear that such enterprises are increasingly expected to exercise something approaching governance responsibilities under a number of circumstances.[36] The ideal of a strict separation between the public obligations of states and the private obligations of economic actors has essentially disappeared in some of these contexts.[37]

However, more precisely relevant is the example of the socially

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v. Mich. Chamber of Commerce, 494 U.S. 652 (1990) (no corporate constitutional right to use corporate funds to support candidates in elections for pubic office).

33. *See, e.g.*, Patrick J. Keenan, *Financial Globalization and Human Rights*, 46 COLUM. J. TRANSNAT'L L. 509 (2008).

34. The OECD "brings together the governments of countries committed to democracy and the market economy from around the world" for a variety of development regulatory and harmonization purposes. *See* OECD, ABOUT OECD, http://www.oecd.org/pages/0,3417,en_36734052_36734103_1_1_1_1_1,00.html, (last visited Jan. 12, 2009). 33 nations are currently members of the OECD, including Australia, Austria, Belgium, Canada, Czech Republic, Denmark, Finland, France, Germany, Greece, Hungary, Iceland, Ireland, Italy, Japan, Korea, Luxembourg, Mexico, Netherlands, New Zealand, Norway, Poland, Portugal, Slovakia, Spain, Sweden, Switzerland, Turkey, United Kingdom, and the United States. *See* OECD, RATIFICATION OF THE CONVENCTION ON THE OECD, http://www.oecd.org/document/58/0,3343,en_2649_201185_1889402_1_1_1_1,00.html (last visited Feb. 28, 2009). 11 other states are not members but have adhered to the OECD Guidelines, including Argentina, Brazil, Chile, Estonia, Egypt, Israel, Latvia, Lithuania, Peru, Romania & Slovenia. Halina Ward, *The OECD Guidelines for Multinational Enterprises and Non-Adhering Countries: Opportunities and Challenges of Engagement* 2 (2004), *available at* http://www.oecd.org/dataoecd/6/62/33807204.pdf (last visited Nov. 15, 2009).

35. *See* OECD, OECD Guidelines for Multinational Enterprises (2000), *available at* http://www.berr.gov.uk/files/file46192.pdf. The relevant provisions are discussed *infra* at Section II. Following the adoption of the Revised OECD Guidelines for Multinational Enterprises on the occasion of the OECD's annual Council meeting at ministerial level in Paris on 27 June 2000, the OECD published a booklet which comprises the following elements: revised text and commentary, implementation procedures and the Declaration on International Investment and Multinational Enterprises. The Guidelines can be found online at http://www.oecd.org/dataoecd/56/36/1922428.pdf.

36. This is discussed in Larry Catá Backer, *Rights and Accountability in Development (RAID) v. DAS Air and Global Witness v. Afrimex: Small Steps Toward an Autonomous Transnational Legal System for the Regulation of Multinational Corporations*, 10(1) MELB. J. INT'L L. 258 (2009) [hereinafter Backer, *Rights and Accountability*].

37. *See, e.g.*, *Statement by the United Kingdom National Contact Point (NCP) for OECD Guidelines for Multinational Enterprises: Das Air*, (July 21, 2008), *available at* http://www.berr.gov.uk/files/file47346.doc [hereinafter *U.K. NCP Statement*]; *Final statement by the U.K. National Contact Point for*

conscious private investment fund. These funds have no connection with a state, yet are organized around investment grounded not merely in wealth maximizing, but in creating incentives to promote certain corporate behaviors through investment decisions.[38] To some extent, private funds seek to project governance power to the objects of their investments. And they engage in this activity not merely to maximize wealth but for the importance the members of those funds attach to reforming the behaviors of the targets of their investment activities. In any case, such activity suggests that the model of private investment activity at the heart of SWF regulatory discourse is at best incomplete.

On a more general level of theory, the regulatory private fund and the participatory sovereign wealth fund also suggest that the simple categories on which an understanding of these entities is based—that states and private entities act differently in measurable and quite separable ways—is false. Both sovereign and private funds appear to present private means to accomplish public acts, and private ends as well. In this respect they provide significant evidence of a further erosion of the public/private divide in lawmaking and governance. When states seek to be treated like private entities with respect to certain of their activities, and when private funds seek to assert a regulatory authority with respect to certain of their activities, the old jurisdictional divides between the state and the private sector, between public and private law regimes, must be substantially weakened. In this respect, issues of sovereign wealth fund regulation mirror the larger debates about governance without government[39] and the transformation of the jurisprudential expression of sovereignty.[40]

Sovereign wealth funds, then, represent another wave in the assault on the traditional public/private divide. As corporations assume a

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*the OECD Guidelines for Multinational Enterprises: Afrimex (UK) Ltd*, (Aug. 28, 2008) *available at* http://www.berr.gov.uk/files/file47555.doc [hereinafter *Final Statement*].

38. Consider in that regard funds like TIAA-CREF social choice fund. *See* TIAA-CREF, Social Choice Equity (TICRX) Mutual Fund Profile, http://www.tiaa-cref.org/performance/mutual_funds/profiles/0059.html (retail class) (last visited Dec. 17, 2009); http://www.tiaa-cref.org/performance/retirement/profiles/1617.html (retirement class) (last visited Dec. 17, 2009).

39. *See, e.g.*, B. Guy Peters & John Pierce, *Governance Without Government? Rethinking Public Administration*, 8(2) J. PUB. ADMIN. RESEARCH & THEORY 223, 223-243 (1998).

40. *See, e.g.*, Mark W. Zacher, *The Decaying Pillars of the Westphalian Temple: Implications for International Order and Governance*, *in* GOVERNANCE WITHOUT GOVERNMENT: ORDER AND CHANGE IN WORLD POLITICS 58-101 (James N. Rosenau & Ernst Otto Czempiel eds., Cambridge University Press, 1992); Paul Schiff Berman, *From International Law to Law and Globalization*, 43 COLUM. J. TRANSNAT'L L. 485 (2005).

greater regulatory role,[41] states appear to be assuming a greater private role.[42] Sovereign wealth funds are an important manifestation of those new forms of public/private conflation through instrumentalities and actions that are neither fish nor fowl under the traditional regulatory divisions. Sovereign wealth funds thus serve to show the growing irrelevance of the public/private distinction, and the rise of a new set of questions for law, politics and governance. In that context, the current thrust of regulatory reform—grounded in the assumptions that private and public actors are distinct, that those distinctions can be modeled, and that state investment vehicles might be treated as benign when they adopt the behaviors of this ideal model of private behavior—just does not work. And it does not work precisely because public actors cannot wholly escape their character as sovereigns, and private entities engage in regulatory activities through private markets.

All of these trends and challenges are nicely exposed in the form of one type of emerging sovereign wealth fund, the socially responsible sovereign wealth fund. This article focuses on a close review of one of the most influential of this type of sovereign wealth fund, the Norwegian sovereign wealth funds.[43] Together they are among the largest and most influential sovereign wealth funds in the world, and the largest in Europe. The International Monetary Fund indicates that Norway's Government Pension Fund—Global is one of the largest and fastest growing SWFs in the world with total assets amounting to $373 billion at the end of 2007, which represents nearly 100 percent of Norway's

41. *See, e.g.*, Errol Meidinger, *Multi-Interest Self Governance Through Global Product Certification Programs* (Buffalo Legal Studies Research Paper Series, Paper No. 2006-016, 2006), *available at* http://ssrn.com/abstract=917956; Backer, *Objects and Sources*, *supra* note 2.

42. *See, e.g.*, Jean-Philippe Robe, *Multinational Enterprises: The Constitution of a Pluralistic Legal Order*, *in* GLOBAL LAW WITHOUT A STATE 45, 45-47, 52-56 (Gunther Teubner ed. 1997).

43. The Norwegian government actually operates multiple funds with distinct investment obligations. One of the funds is focused on domestic investment and is tied more closely to the pension obligations of the state and the other is directed toward outbound investment. "In December 2005, the Storting adopted the Act relating to the Government Pension Fund, and the Government Pension Fund—Global and the Government Pension Fund—Norway were established on the basis of the assets of the Government Petroleum Fund and National Insurance Scheme Fund, respectively. Folketrygdfondet was charged with managing the assets of the Government Pension Fund—Norway on behalf of the Ministry of Finance." FOLKETRYGDFONDET, OWNERSHIP REPORT 2007 1, *available at* http://www.ftf.no/r/fil/2007123_1.pdf (last visited Dec. 17, 2009). The focus of this article is on the Government Pension Fund—Global. "The fund is commonly referred to as The Petroleum Fund (Norwegian: Oljefondet)." Sovereign Wealth Fund Institute, *Government Pension Fund—Global*, http://www.swfinstitute.org/fund/norway.php (last visited Dec. 17, 2009). The organization and functioning of these entities is discussed, infra, at Section III.

GDP.[44]

The article first describes conceptual and regulatory frameworks on which current policy discussions of sovereign wealth funds are undertaken.[45] It develops the context in which the public/private distinction is elaborated and used as a framework for rules that permit access of sovereign wealth funds to private markets as long as they restrict their activities to those that mimic a certain set of idealized private market behaviors. Section II then turns to the Norwegian funds themselves, focusing on the history of these funds, their legal structure, and the development of their investment principles.[46] This review fleshes out the contours of a model sovereign wealth fund that appears to conform to the emerging consensus—sovereign in form and private in practice. And it contextualizes the ethical component of investment within this framework. Section IV then examines the Fund in action.[47] This examination concentrates on the investment effects of the Fund in two principal areas: corporate social responsibility/ethics, and development and use of the Fund to advance state macroeconomic policy, especially in the aftermath of the global economic crisis after 2008.[48]

This examination of fund behavior evidences a substantial ambiguity—it operates like a private investment fund to the extent that it seeks to maximize shareholder value, but the maximization of shareholder value in this case requires the Fund be used to acheive the global governance goals of the Norwegian state. Section V of the article turns to the consideration of this ambiguity.[49] Norway's investment portfolios reflect both private participatory behaviors, consonant with private funds, from socially conscious to more politically directed wealth management funds. But the funds' activities do more than that as well. They are used quite consciously to serve as an instrument of Norwegian state policy in its intervention in issues of regulation of transnational corporations and in the fashioning of governance and behavior norms for economic entities generally.[50]

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44. *See* Velculescu, *supra* note 7.

45. *See infra* Section II.

46. *See infra* Section III.

47. *See infra* Section IV.

48. *See infra* Section IV. For this purpose, the actions of the Fund will be examined as it developed with respect to shareholder activism in the context of corporate governance norms, and the response of fund managers to calls for divestment of certain entities engaged in activity in Israel and in Myanmar. Also examined are changes to the Fund's investment strategy after the start of the global economic crisis in 2008.

49. *See infra* Section V.

50. *See infra* Section V.

And this suggests the limits of regulatory policies represented by current approaches to governing SWFs. Sovereign wealth funds like that of Norway are strong examples of the character of these entities as regulatory chameleons. Current regulation is based on a formally public/functionally private model. The touchstone for the model is an 'idealized private investor' that can be distinguished from others. The idealized private investor standard at the heart of sovereign wealth fund soft regulation does not work. But it also does not work for private investment funds from which they are in part derived. For that purpose, the Norwegian Fund is considered against private socially responsible funds. Sovereign wealth funds may mimic private investment not only because private funds engage in regulatory/sovereign investment strategies but also because the public fund mimics wealth or benefit maximizing participatory private commercial activity. The Norwegian funds in action evidence this nicely and point to the need for a different regulatory framework.

## II. Conceptual and Regulatory Framework: Public Actors and Private Action

Like much else about sovereign wealth funds, there is little consensus on a definition.[51] The differences in definition reflect the ambiguity of the instrument itself—formally sovereign yet functionally private. It also reflects the further ambiguity even with respect to function—again traditionally sovereign but now also more aggressively private.[52] But underlying the ambiguities, and the means to overcome them, is a fidelity to a strict distinction between public and private law and actors. It is this combination of fidelity to the public/private divide combined with an exploitation of the formally public-functionally private character of sovereign wealth funds, that serves as the foundation for regulatory approaches to sovereign wealth funds. This section explores the connection between the definition of sovereign wealth funds that

51. *See, e.g.*, Jen, *supra* note 3.

52. Thus, "[r]ather than being well defined and distinct from other types of funds, there is a great deal of overlap between SWFs and their close cousins," official reserves and pension funds. *Id.* at 3. As late as 2005, Andrew Rozanov could describe sovereign wealth funds as a by-product "of national budget surpluses, accumulated over the years due to favourable macroeconomic, trade and fiscal positions, coupled with long-term budget planning and spending restraint. Usually, these funds are set up with one or more of the following objectives: insulate the budget and economy from excess volatility in revenues, help monetary authorities sterilise unwanted liquidity, build up savings for future generations, or use the money for economic and social development." *See* Rozanov, *supra* note 4, at 1.

privilege its sovereign character, the positing of an oppositional entity (the private wealth investment entity), the extraction of a set of characteristics that distinguish the private investment entity from regulatory investing, and the proffering of a rule that would forego special regulation of functionally private sovereign investment entities. Critical to this regulatory enterprise is the construction of an idealized private investor, against which sovereign wealth management can be assessed.

The simplest definitions pick up the first thread of this regulatory construction, reflecting as well the conservative inertia of this conceptual framework: "What I have in mind is a government investment vehicle that manages foreign assets with a higher risk tolerance and higher expected returns than for central bank foreign currency reserves."[53] U.S. officials have sought to define these entities by emphasizing the public nature of these investment instruments. An SWF has been understood to include "a government investment vehicle which is funded by foreign exchange assets, and which manages those assets separately from official reserves."[54] This definition has won some acceptance in the private U.S. financial community.[55] The IMF also focuses on the public character of the ultimate owner of the fund. Thus IMF studies would define sovereign wealth funds to include "government-owned investment funds, set up for a variety of macroeconomic purposes. They are commonly funded by the transfer of foreign exchange assets that are invested long term, overseas."[56] Work produced through the OECD has also emphasized the public character of the entity. For example, "Sovereign Wealth Funds (SWFs) are defined as pools of assets owned and managed directly or indirectly by govern-

53. Sir John Gieve, Deputy Governor of the Bank of England, Speech at the Sovereign Wealth Management Conference in London: Sovereign Wealth Funds and Global Imbalances 1 (May 14, 2008), *available at* www.bis.org/review/r080319d.pdf.

54. Clay Lowery, Acting Under-Sec'y of the Treasury, Remarks on Sovereign Wealth Funds and the International Financial System (June 21, 2007), *available at* http://www.ustreas.gov/press/releases/hp471.htm.

55. *See* Jen, *supra* note 3, at 2 (a SWF has five ingredients; they are sovereign, a high foreign currency exposure, no explicit liabilities, a high risk tolerance, and a long investment horizon).

56. INT'L MONETARY FUND, SOVEREIGN WEALTH FUNDS—A WORK AGENDA 4 (Feb. 29, 2008) (prepared by the Monetary and Capital Markets and Policy Development and Review Departments and approved by Mark Allen and Jaime Caruana), *available at* https://www.imf.org/external/np/pp/eng/2008/022908.pdf. Annex II to this document provides short definitions provided by other stakeholders in the financial system, from Deutsche Bank ("financial vehicles owned by states which hold, manage, or administer public funds and invest them in a wide range of assets") to Morgan Stanley ("An SWF needs to have five ingredients: sovereign; high foreign currency exposure; no explicit liabilities; high-risk tolerance; and long-term investment horizon"). *Id.* at 37-38.

ments to achieve national objectives."[57] More to the point is a definition that looks only to the responses these entities have on states: "Sovereign wealth funds (SWFs) are government-controlled investment vehicles which recently have stimulated protectionist sentiments in some OECD countries."[58]

But the definition most likely to be influential in the coming years is that of the International Working Group of Sovereign Wealth Funds,[59] the group that produced the Santiago Principles.[60] The International Working Group of Sovereign Wealth Funds (IWG) defines Sovereign Wealth Funds as:

> special purpose investment funds or arrangements, owned by the general government. Created by the general government for macroeconomic purposes, SWFs hold, manage, or administer assets to achieve financial objectives, and employ a set of investment strategies which include investing in foreign financial assets. The SWFs are commonly established out of balance of payments surpluses, official foreign currency operations, the proceeds of privatizations, fiscal surpluses, and/or receipts resulting from commodity exports."[61]

The IWG was clear that the definition contained three key elements: ownership, investments, and purposes and objectives.[62] Ownership

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57. ADRIAN BLUNDELL-WIGNALL, YU-WEI HU & JUAN YERMO, SOVEREIGN WEALTH AND PENSION FUND ISSUES (Apr. 25, 2008), http://www.oecd.org/dataoecd/27/49/40196131.pdf. The OECD has been extremely active in the SWF front, including numerous articles; the above is one definition among many OECD published reports.

58. HELMUT REISEN, ORGANIZATION FOR ECONOMIC CO-OPERATION & DEVELOPMENT, HOW TO SPEND IT: COMMODITY AND NON-COMMODITY SOVEREIGN WEALTH FUNDS 5 (2008), http://www.oecd.org/dataoecd/41/3/41412391.pdf.

59. The International Working Group of Sovereign Wealth Funds "was established at a meeting of countries with SWFs on April 30-May 1, 2008 in Washington D.C: At the meeting it was agreed that the IWG would initiate the process, facilitated and coordinated by the International Monetary Fund." *Santiago Principles*, *supra* note 8, at 1. The IWG consisted of 26 countries, including the United States and Canada, as well as permanent observers, including the OECD and the World Bank. Most of the IWG countries had SWFs. *See id.*

60. *See id.*

61. *Id.* at 27, Appendix I (defining sovereign wealth funds) (emphasis removed).

62. *Id.* The IWG limited SWFs to those vehicles owned by the general government of a state, including central and subnational governments. *Id.* The IWG understood "investment strategies [to] include investments in *foreign financial assets*, so it excludes those funds that solely invest in domestic assets." *Id.* The IWG defined the latter as "financial objectives." *Id.* It is this framework that will move us conceptually from state vehicle to acceptance as a private entity in function.

provides the basis for establishing the character of the entity, investments provide the trigger for regulation—the projection of fiscal power abroad. Purposes and objectives provide the framework for regulation based on functional performance.

The principal common feature of all sovereign wealth funds is their ultimate connection to a public sovereign, understood to be a nation state, but not necessarily limited to such an organization.[63] The key connection is between that state and its need to manage its assets. That management implies both a need for diversification among risk pools and a strong connection to macroeconomic (and sovereign) concerns. The characteristics of the entity are then derived from that owner, the most fundamental of which is the objective of the fund, for macroeconomic purposes. This suggests a crucial and perhaps insurmountable distinction between private funds and public funds. The former are presumed to be grounded ultimately in wealth maximization objectives for its owners. The latter is hardly constrained by such objectives, though they may provide a subset of objectives, based in part on the source of funds—excess funds not to be spent immediately to fund government operations or programs. Thus, the potential implication that sovereign wealth funds may well be regulatory vehicles operating in the private sector is softened. The definition also suggests that this fundamental macroeconomic objective is, in fact, limited to achieve financial objectives, though not necessarily commercial objectives. Yet the object is to ensure that such funds are not treated differently than similarly constituted funds held by private interests.[64]

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63. There is no reason to suggest that sovereign wealth funds lose their character as such merely because the owner of such a fund is a public entity that is not a sovereign. An easy example would be a sovereign wealth fund owned by the European Union, a supra-national organization that is not a political sovereign in the traditional sense. For a discussion of the constitution of the European Union, *see, e.g.*, J.H.H. WEILER, THE CONSTITUTION OF EUROPE: 'DO THE NEW CLOTHES HAVE AN EMPEROR?' AND OTHER ESSAYS ON EUROPEAN INTEGRATION 286-323 (Cambridge University Press 1999). More interesting would be a sovereign wealth fund owned by a different form of supra-national organization with recognized legal personality—for example a regional trade organization like ALBA. For a discussion of ALBA, *see, e.g.*, Larry Catá Backer & Augusto Molina, *Cuba and the Construction of Alternative Global Trade Systems: ALBA and Free Trade in the Americas* (May 2009) (unpublished working paper on file with author).

64. Thus, for example, the co-chair of the International Working Group of Sovereign Wealth Funds Group, H.E. Hamad Al Hurr al-Suwaidi, declared: "Moreover, in the Santiago Principles, there are provisions confirming the IWG's expectations that recipient countries will not subject the SWFs to discriminatory measures to which other foreign or domestic investors in similar circumstances are not subjected. We trust the recipient countries will support these provisions." H.E. Hamad Al Hurr al-Suwaidi, Statement at a Meeting of the International Monetary and Financial Committee of the International Working Group of Sovereign Wealth Funds Group in

Public ownership, bent to some ill-defined scope of public purpose and tied to the desires of the public owner, serves as the framework from which forays into more elaborate definitions of the entity are attempted. Better put, perhaps, at this point the routine of categorization often substitutes for engagement with definition in discussion of sovereign wealth funds. The categories are also well established. Sovereign wealth funds tend to be defined with more precision by reference to their specific investment purpose (beyond the generic obligation to satisfy their owners), their organization, the sources of their funds, or some combination thereof. Thus, for example, International Monetary Fund studies have distinguished among these funds on the basis of their distinctly sovereign objectives, distinguishing among five objectives-oriented funds.[65]

This is a framework used in other studies as well. For example, such entities have been defined as "a state-owned or influenced fund that obtains its funding from foreign-currency reserves or commodity export revenues, though in certain instances, government budget surpluses and pension surpluses have also been transferred to SWFs."[66] The World Bank has suggested that these entities are "long-term investment fund[s], typically for both income and intergenerational wealth transfer . . . ."[67] More starkly put, sovereign wealth funds are

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Washington, D.C. 5 (Oct. 11, 2008), *available at* http://www.iwg-swf.org/pubs/eng/imfciwg.pdf (last visited Mar. 2, 2009). *See infra* at Section IV.

65. INT'L MONETARY FUND, *supra* note 56, at 5.

> Five types of SWFs can be distinguished based on their main objective: (i) stabilization funds, where the primary objective is to insulate the budget and the economy against commodity (usually oil) price swings; (ii) savings funds for future generations, which aim to convert nonrenewable assets into a more diversified portfolio of assets and mitigate the effects of Dutch disease; (iii) reserve investment corporations, whose assets are often still counted as reserve assets, and are established to increase the return on reserves; (iv) development funds, which typically help fund socio-economic projects or promote industrial policies that might raise a country's potential output growth; and (v) contingent pension reserve funds, which provide (from sources other than individual pension contributions) for contingent unspecified pension liabilities on the government's balance sheet.

*Id.*

66. *See, e.g.*, Greene & Yeager, *supra* note 15, at 248-49 (distinguishing between "(i) central banks, (ii) stabilization funds, (iii) public pension funds, (iv) government investment companies, and (v) state-owned enterprises").

67. *See* "As Simon Johnson, Director of Research for the IMF writes, "sovereign wealth funds are a fairly new name for something that's been around for quite a while: assets held by

defined by reference to the greatest difference between the public and private sectors—the need to maximize the wealth of shareholders. "An SWF is a global investment fund owned by a government. Unlike a private international investment fund, which is governed by profit motives, SWF's might have national strategic objectives that have made them controversial investment vehicles."[68]

Most broad, perhaps, is the approach of the United Nations: "Sovereign wealth funds seek to diversify foreign exchange assets and earn a higher return by investing in a broad range of asset classes. Typical asset classes are longer-term government bonds, asset backed securities, corporate bonds, equities, commodities, real estate, derivatives, alternative investments, and foreign direct investment."[69] U.S. officials have distinguished between two large categories of SWFs, commodity and non-commodity funds.[70] Yet as we can now better understand, the large variety of forms that sovereign wealth investing can take does not alter the fundamental characteristic of the entity as sovereign.[71] And, indeed, quibbles over the form or organization of funds tend to be viewed as incidental.[72] Yet, it is well to remember, though, that the organization of sovereign wealth funds can be as complicated as any other global economic enterprise. The sovereign wealth fund can serve as the single investment entity, organized as a corporation or similar enterprise under the general law of its sovereign owner[73] or more

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governments in another country's currency". Sovereign Wealth Funds, *Sans Poverty North American Affairs News*, World Bank 13 (Mar. 13, 2008).

68. Sanjiv Shankaran, *Norway Fund to Put $2 Bn in India*, LIVEMINT.COM, Oct. 22, 2008, http://www.livemint.com/swf.htm (last visited Dec. 20, 2009).

69. U.N. Econ. & Soc. Comm'n for Asia & the Pacific [ESCAP], Poverty & Dev. Div., *Key Economic Developments and Prospects in the Asia-Pacific Region 2008*, U.N. Doc. ST/ESCAP/2461 (2007), *available at* http://www.unescap.org/pdd/publications/key2008/key2008.pdf.

70. Lowery, *supra* note 54.

71. This might help explain the Santiago Principles's focus on framework rather than form. *See Santiago Principles*, *supra* note 8, at 7, (GAPP 1 Principle). The Santiago principles identify three broad approaches—SWFs established as a separate legal identity, SWFs established as state owned corporations, and SWFs established as a pool of assets without separate legal personality. "Provided that the overall legal framework is sound, each of these structures can be employed to meet the requirements laid down in this Principle." *Id.* at 11-12.

72. *See, e.g.*, Edwin M. Truman, *A Blueprint for Sovereign Wealth Fund Best Practices*, Peterson Institute for International Economics, Policy Brief No. PB08-3 (April 2008), www.ciaonet.org/pbei/iie/0001182/0001182.pdf.

73. For example, the Abu Dhabi Investment company was founded "on February 24, 1977 as the first U.A.E. investment company in the capital. ADIC is a Joint Stock Company that specializes in providing investment and corporate finance in addition to advisory services. ADIC is jointly owned by the Abu Dhabi Investment Authority and the National Bank of Abu Dhabi (2%)." SWF

typically organized pursuant to special legislation.[74] But sovereign wealth funds can themselves serve as the holding company for any number of vertically or horizontally organized sub-funds, through which the actual operations of the entities are realized. These sovereign wealth enterprises can include any form of economic enterprise, from investment to operating entities.[75]

From these forays through thin thickets of definition, it is possible to discern a common set of assumptions that are shared about the nature of the creature defined—the sovereign wealth fund—and the assumptions that the definition is meant to embrace. The first is the focus on ownership. The organization of the fund itself is not interesting—its owners are. The emphasis is on the sovereign, less on its wealth, and only later on the fund.[76] They are a form of state sovereign activity, the preservation of public wealth. "In contrast to these other forms of government assets, SWFs typically seek riskier investments and a higher rate of return. Ostensibly, they are run purely to increase the wealth of the state, not to pay off any specific debt."[77] This focus leads to conceptual conundrums, a principal one of which is the character of state owned enterprises. These entities are operating companies. But they are owned by states. When they purchase other businesses, or invest in them abroad, they appear to function like sovereign wealth

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Institute, Abu Dhabi Investment Authority, http://www.swfinstitute.org/fund/adia.php (last visited Nov. 13, 2009).

74. The Norwegian funds were created in this manner. *See* discussion *infra* Section III.

75. Some have, for example, identified the China National Offshore Oil Corporation and the Dubai DP World as sovereign wealth enterprises. *See, e.g.*, Press Release, KPMG, Sovereign Wealth Funds—The New Global Investors (Oct. 1, 2008), *available at* http://www.kpmg.ch/docs/MR_Sovereign_Wealth_Funds_01102008_ENS.pdf. *See also* Sovereign Wealth Fund Institute, Sovereign Wealth Enterprise Frequently Asked Questions, http://www.swfinstitute.org/research/swe.php (last visited Nov. 23, 2009) (suggesting that SWEs may be created for flexibility, stating "[a] sovereign wealth fund could have a strict investment mandate in place; however, the sovereign wealth enterprise has its own rules. For instance, many public pension funds are unable to short stocks. To get around this they can hire an external manager to manage a portfolio that could have a long-short strategy. A second reason could be transparency. If a sovereign wealth fund has hundreds of sovereign wealth enterprises, it is harder to track their holdings. Lastly, is to avoid being lumped into the same category as a sovereign wealth fund and avoid the public spotlight"); On the China National Offshore Oil Corp., *see* Company Description, TradeBig.com, http://www.7621.tradebig.com (last visited Nov. 23, 2009); China National Offshore Oil Corp. Company Overview, http://en.cnooc.com.cn/data/html/english/channel_110.html (last visited Nov. 23, 2009).

76. Thus, for example, the IWG definition of SWFs incorporate these notions. *See supra* note 61.

77. Lee Hudson Teslik, *Backgrounder: Sovereign Wealth Funds*, Council on Foreign Relations (Jan. 29, 2009), http://www.cfr.org/publication/15251 (last visited Nov. 13, 2009).

funds—but only if you privilege the ownership aspect over everything else.[78]

The second is the conflation of ownership and the entity itself. In a sense the focus on fund objectives serves to cement the unity of ownership and entity. The owners of sovereign wealth funds are joined to the funds they own in ways that would be a matter of indifference where owners are non-state actors. And, indeed, legal distinctions—including the distinctions between legal persons and sovereign persons—ought to be disregarded.[79] There is an assumption that the owner and fund are joined in ways that, in other circumstances, might suggest a viable case for piercing the corporate veil.[80] This assumption can be understood as part of a larger transnational law project that has as its aim the substitution of notions of complicity and regulatory guardianship for the independence of juridical persons and the limits of their role to purely private economic activities.[81] This is evident in regulatory constructs like the OECD's Risk Awareness Tool for Multinational Enterprises in Weak Governance Zones.[82] But however characterized, the role envisioned is regulatory rather than participatory. The entity in effect is presumed to be required to substitute its apparatus for that of the (missing) state.

An inverse relationship of sorts applies to states seeking entry into private markets. The state's expression as a juridical personality, perhaps separately constituted from its instruments as they proceed abroad, is also amalgamated with its instruments, however constituted. And,

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78. Greene and Yeager suggest that these vehicles "may be the most problematic from an investee-country's perspective, particularly when the acquirer and the target are infrastructure companies, because the investments may be seen as a means for gaining political leverage." Greene & Yeager, *supra* note 15, at 253. For example, they point to the investment activities of Dubai Ports World and the China National Offshore Oil Company. *Id.* at 253-54.

79. U.S. courts had articulated this idea nearly a century ago. *See* Australian Central Bank O.D. 628, 3 C.B. 124 (1920) (using the language of corporate veil piercing to suggest that an Australian bank was effectively the mere instrumentality or alter ego of the chartering state).

80. For a discussion in the context of mixed field systems of corporate governance, see Backer, *United Nation's Norms, supra* note 2.

81. This is most evident in soft law regimes like that of the OECD. *See* discussion *supra* notes 35-38 and accompanying text.

82. *See* OECD, *OECD Risk Awareness Tool for Multinational Enterprises in Weak Governance Zones* (2006), *available at* www.oecd.org/dataoecd/26/21/36885821.pdf. The explanatory materials explain the relationship between people, state and entity in weak governance zones: "The *Tool* is based on the premise that a durable exit from poverty will need to be driven by the leadership and the people of the countries concerned—only they can formulate and implement the necessary reforms. Companies play important supporting roles and this *Tool* seeks to raise awareness of these roles and to help companies play them more effectively." *Id.* at 9.

indeed, there is a sense that the owner, the state, is itself merely a fiduciary for the greater or ultimate owner—the citizens of each state. Sovereign wealth fund definitions are not focused merely on the sovereign owners. They are also focused on the character of the investments that these funds manage. The funds, like its owners, are "special" in the sense that neither conforms to the default characteristics of the usual actors in markets for investment in non-sovereign entities. In this sense, under emerging notions of transnational governance, both states and multinational corporations are treated similarly—both become bound up in significant regulatory networks of complicity.

And thus the third assumption: sovereign wealth funds are presumed to serve as flow-through entities, at least with respect to fund objectives.[83] This becomes important because of the underlying assumption that sovereigns do not behave like non-state actors.[84] Where sovereigns seek to participate in markets or other activities along with non-state actors, the assumption is that they do so for reasons and goals irrelevant to other actors. Where markets are founded on assumptions of common objectives, it might follow that the appearance of sovereigns in those markets might effectively subvert them. In the case of sovereign wealth funds, the critical assumption is that, unlike private actors, the owners of sovereign wealth funds are not constrained by a "profit" motive.[85]

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83. There is an important distinction, of course, between the idea of flow-through activity with respect to *legal consequences* such as piercing the corporate veil, *see, e.g.*, John H. Matteson, *The Modern Law of Corporate Groups: An Empirical Study of Piercing the Corporate Veil in the Parent-Subsidiary Context*, 87 N.C. L. REV. 1091 (2009), and the idea of conflation of purpose that attaches to understandings of the operations of sovereign wealth funds and produces *regulatory consequences*. *See* Justin O'Brien *Barriers to Entry: Foreign Direct Investment and the Regulation of Sovereign Wealth Funds*, 42 INT'L LAW. 1231, 1239-40 (2008); Jason Buhi, *Negocio de China: Building Upon the Santiago Principles to Form an Effective International Approach to Sovereign Wealth Fund Regulation*, 39 HONG KONG L.J. 197 (2009).

84. Thus, as the New York Bar Association Tax Section Report noted, "Treasury's recent advocacy of the SWF 'Code of Conduct' and renewed interest in strategically important assets suggest that the policy issues raised by the new prominence of SWFs are *not* that they are engaged in profit-maximizing investment activities that could somehow benefit unfairly from a tax exemption intended for 'governmental' activities, but rather that SWFs could be used to further governmental political agendas." NEW YORK STATE BAR ASSOCIATION TAX SECTION, REPORT ON THE TAX EXEMPTION FOR FOREIGN SOVEREIGNS UNDER SECTION 892 OF THE INTERNAL REVENUE CODE 23 (June 2008), *available at* http://www.nysba.org/AM/Template.cfm?Section=Tax_Section_Reports_2008&TEMPLATE=/CM/ContentDisplay.cfm&CONTENTID=28867 (follow "Tax Report 1157" hyperlink).

85. *Id.* at 10-16.

These assumptions serve as the framework for regulatory approaches to sovereign wealth funds in host states, as well as in current efforts to create a transnational regulatory framework for sovereign wealth funds.[86] Traditional sovereign investment practices were understood as both conservative and "political." In the form of sovereign wealth funds, these instruments could be understood as more risk tolerant in their appetite for investment vehicles but also "political" in a similar way. Yet because the range of investments could be substantially broader, the consequences of the "political" objectives of the use of state assets, especially when projected abroad, could be viewed as invasive by host states.[87] Or they can be understood as a proxy for dictatorship within home states.[88] But in either case they might be feared as threatening in a way that private funds are not. And it all ties back into the sovereign requirements of the owners of those funds. "Certain international reserves are always needed. . . . However, sovereign wealth funds are something different. They reflect a paternalistic—and economically illiterate—notion that the ruler knows best while citizens are so irresponsible that they cannot be entrusted with their own savings. It would be more economical and democratic to cut taxes and let citizens save and invest themselves."[89]

SWFs thus proceed from definition to conundrum. If SWFs are grounded in the reality of their formal connection to states, and if states are deemed sovereign in their actions, then it might be reasonable to assume that such funds could not be treated like private investment funds. To bridge that gap, it was necessary to find a way to

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86. The regulatory schemes are discussed in Backer, *Regulatory Responses, supra* note 11.

87. This is nicely described in Kimmitt, *supra* note 4.

88. One commentator sought to assuage the fears of sovereign wealth funds in host states by igniting fears of those instruments among citizens of home states:

> In truth, such funds are nothing for Americans or Europeans to fear. If anyone should worry about them, it's the people whose governments are amassing them. That's because governments tend to be terrible at managing money that is best left in the hands of private citizens. And locking away billions of dollars in wealth can have pernicious economic side effects. Maybe that's why sovereign wealth funds are popular with dictators and semi-authoritarian regimes, which don't have to answer for the consequences when they make poor economic gambles.

Anders Åslund, *The Truth About Sovereign Wealth Funds,* FOREIGN POLICY, Dec. 2007), http://www.foreignpolicy.com/story/cms.php?story_id=4056 (last visited March 30, 2009). *See also* Victor Shih, *Tools of Survival: Sovereign Wealth Funds in Singapore and China,* 14(2) GEOPOLITICS 238 (2009) (role of political unity in directling SWF activity in authoritarian regimes).

89. Aslund, *supra* note 88.

disconnect SWFs from the state and sovereign activity, and to model private activity in a way that made it possible to construct a set of behavior principles that might produce equivalence between SWFs and private investment vehicles. The first was accomplished by creating a functional distinction between state and SWF, a distinction unnecessary for traditional sovereign investment. The second was grounded in the presumption that private investment has no regulatory component and that there is a way of distilling the essence of private investment behaviors sufficiently precisely to distinguish those behaviors from sovereign conduct. Both are nicely captured in the Santiago Principles. Both are problematic either as concept or in application.

Separation of sovereign from investment entity can be accomplished at something like a functional level. That requires the invocation of a legal framework in which there can be created some sort of legal separation between state and investment entity.[90] This separation, though to some extent formally constituted, is essentially functional—states are as free to discard formal distinctions by legislative or other action as they are free to create them in the same way. This separation includes a disclosure[91] and transparency[92] element. "The governance framework for the SWF should be sound and establish a clear and effective division of roles and responsibilities."[93] The state is to be treated more like a shareholder or investor participant in a private investment fund than as a regulatory sovereign.[94]

Once free of an intimate connection with the political apparatus of the state, the functionally private and privately ruled SWF is meant to exercise its investment strategies according to a non-sovereign, apoliti-

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90. *See, e.g.*, *Santiago Principles*, *supra* note 8, at 7, GAPP 1-5 Principles.

91. *See id.* GAPP 4 Principle, which encourages the public disclosure of "policies, rules, procedures, or arrangements in relation to the SWF's general approach to funding, withdrawal and spending operations."

92. *See, e.g.*, *id.* GAPP 1-5 Principles.

93. *Id.* GAPP 6 Principle (the object is to "facilitate accountability and operational independence in the management of the SWF"). The explanatory notes emphasize the importance of functional separation of entity/investment pool from the state apparatus even where the SWF does not have a separate legal personality under municipal law. "In such cases, it is important that there be a clear distinction between the owner/governing body(ies) and the agency responsible for the operational management of the SWF." *Id.* at 15, GAPP 6 Principle, Explanation and Commentary.

94. "The Owner should set the objectives of the SWF . . . and exercise oversight over SWF operations." *Id.* GAPP 7 Principle. The governing bodies are meant to act in a way similar to that of a board of directors of a private enterprise. "The governing body(ies) should act in the best interests of the SWF, and have a clear mandate and adequate authority and competency to carry out its functions." *Id.* at 16, GAPP 8 Principle, Explanation and Commentary.

cal model. "The SWF's investment decisions should aim to maximize risk-adjusted financial returns in a manner consistent with its investment policy."[95] Likewise, SWF management, and especially "[d]ealings with third parties for the purpose of the SWF's operational management should be based on economic and financial grounds."[96] Economic and financial grounds are set as the base line for SWF operation. "If investment decisions are subject to considerations (other than economic and financial considerations, these should be clearly set out in the investment policy and be publicly disclosed."[97] This suggests both the focus of functional operation, and the inability to completely eliminate the sovereign element from investment.[98] The compromise is not regulation but disclosure.[99]

Functional separation suggests the possibility that a sovereign can structure part of its apparatus to operate like a private entity. A core element of that functionally private operation norm focuses on the privileging of the "economic and financial considerations" investment policy for SWFs, described above. There are three other parts. The first is information equality. "The SWF should not seek or take advantage of privileged information or inappropriate influence by the broader government in competing with private entities."[100] The second is the power of sovereign investment entities to participate in the governance of those entities in which it has invested. "SWFs view shareholder ownership rights as a fundamental element of their equity investments' value."[101] Here again, the functional separation of sovereign and SWF

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95. *Id.* at 8, GAPP 19 Principle.

96. *Id.* GAPP 14 Principle.

97. *Id.* at GAPP 19.1 Subprinciple.

98. "The SWF's operations can have a significant impact on public finances, monetary conditions, the balance of payment, and the overall sovereign balance sheet. Thus, operations of the SWF that have significant macroeconomic implications should be executed in coordination and consultation with the competent domestic authorities." *Id.* at 13, GAPP 3 Principle, Explanation and Commentary.

99. Disclosure is a powerful element in this case, shifting power to the host states to regulate such nonconforming SWFs in ways that would not be warranted for other conforming SWFs. Again, the idea is to establish a functionally private entity, entitled to a privileged regulatory framework, but permitting non-conforming SWFs to be created, but regulated separately. "The core principle that SWFs' overarching objective is to maximize risk-adjusted financial returns, given the risk tolerance level of the owner." *Id.* at 13, GAPP 19 Principle, Explanation and Commentary.

100. *Id.* at 8, GAPP 20 Principle. "This principle promotes the fair competition of SWFs with private entities. For example, SWFs should not seek advantages such as those arising from privileged access to market sensitive information." *Id.*

101. *Id.* at 9, GAPP 21 Principle.

is solidified by suggesting that such shareholder rights cannot be used to further the political agendas of the sovereign owner of the SWF. "If an SWF chooses to exercise its ownership rights, it should do so in a manner that is consistent with its investment policy and protects the financial value of its investments."[102] This requirement is deepened with a strong disclosure requirement.[103] The object, of course, is to come close to mandating behaviors which mimic private funds.

The third part is perhaps the most important functional distancing of sovereign from fund. "SWF operations and activities in host countries should be conducted in compliance with all applicable regulatory and disclosure requirements of the countries in which they operate."[104] Compliance includes following all municipal laws generally applicable to private investment funds, including those in connection with investigations or any other regulatory actions.[105] In return, the "SWF expects that host countries will not subject the SWF to any requirement, obligation, restriction, or regulatory action exceeding that to which other investors in similar circumstances may be subject."[106] The ultimate concession to private equivalence, of course, is loss of sovereign immunity and special tax status, both of which are apparently now to be exercised in the discretion of host states, and subject to the balancing of the needs of those states for SWF investment over its need to avoid losing that investment through unpopular legislation.

The regulatory "deal" becomes clear now. Sovereign wealth funds are formally sovereign. They may be detached from the state and, to the extent that they operate as functionally private, they may hope to be treated like other private investment vehicles and participate in global financial markets, especially those beyond the borders of their sovereign owners.[107] The characteristics of behaviors constituting private investment activity are also described, at least in general terms. These include investment activity based on economic and financial grounds, a willingness to be subject to the general laws applicable to private

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102. *Id.* "To dispel concerns about potential noneconomic or nonfinancial objectives, SWFs should disclose *ex ante* whether and how they exercise their voting rights." *Id.* at 23, GAPP 21 Principle, Explanation and Commentary.

103. *See id.* at 22, GAPP 21 Principle, Explanation and Commentary.

104. *Id.* at 8, GAPP 15 Principle.

105. *See id.* at 19, GAPP 15 Principle, Explanation and Commentary.

106. *Id.*

107. *See* OECD INVESTMENT COMMITTEE, SOVEREIGN WEALTH FUNDS AND RECIPIENT COUNTRY POLICIES, (Apr. 4, 2008) ("Although the OECD work focuses on host country policies, observance by SWFs of high standards of transparency, risk management, disclosure and accountability can affect the political and policy environment in which recipient countries act.").

investment entities of similar character, restriction on the use of privileged information not generally available to the market, and an assertion of shareholder rights consistent with maximizing economic and financial objectives. The behaviors are meant to describe the universe of conduct that defines private investment activity.

But the regulatory "deal" is dependent on two critical assumptions. The first is that sovereign wealth funds actually behave as formally sovereign and functionally private entities. The second is that the model of private investment fund behavior actually mirrors the reality of that behavior. The SWF that behaves in a way that projects state power—and effectively serves as an instrument of state political activity through private markets would suggest that the consensus model of SWFs as benign entities might not be accurate. Likewise, the private investment vehicle that acts politically—that is that does not conform to the model of investor behavior on which the Santiago Principles are based—suggests that a regulatory model based on depolitization of state activity using a private behavior model is unlikely to accomplish its goal. Yet that very expectation that private enterprises engage in regulatory or governance activity within the sphere of their economic activities has become a hallmark of the current consensus about the nature of private enterprises.[108] That understanding of the wider role of economic enterprises has produced the start of a consensus that such private entities ought to be bound, like states, to a large body of hard and soft law traditionally applied only to states.[109]

So just at the time that regulators press on states a model of private

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108. *See* Special Representative of the Secretary-General on the issue of human rights and transnational corporations and other business enterprises, *Protect, Respect and Remedy: a Framework for Business and Human Rights*, 14-22, *delivered to the Human Rights Council*, U.N. Doc A/HRC/8/5 (April 7 2008), *available at* www.reports-and-materials.org/Ruggie-report-7-Apr-2008.pdf. "With power should come responsibility, and international human rights law needs to focus adequately on these extremely potent international non-state actors." David Weissbrodt & Muria Kruger, *Norms on the Responsibilities of Transnational Corporations and Other Business Enterprises With Regard to Human Rights*, 97 AM. J. INT'L L. 901, 901 (2003) (emphasis added) (referencing in part Mary Robinson, High Comm'r for Human Rights, Second Global Ethic Lecture at The Global Ethics Foundation, University of Tübingen, Germany (Jan. 21, 2002)).

109. As one prominent commentator put it:

> First, legal compliance is inherently problematic at the global level due to the absence of centralized enforcement mechanisms. . . . Second, no less of an authority than Amartya Sens warns against viewing human rights primarily as what he calls 'proto legal commands' or 'laws in waiting.' . . . Third, individual legal liability regimes alone in any case connote solve the structural problem of inadequate protection and fulfillment of human rights. . . .

behaviors that posit a narrow focus of objectives—centered on maximizing financial and economic value—regulators are also pressing on those very private actors a regime of regulation that posits that their behaviors must necessarily be considered in some important measure regulatory and sovereign. This tension between expectation and reality, between visions of conformity to private behavior arising under SWF regimes and other private governance frameworks suggests that regulatory models that presume that private actors behave solely to promote purely financial or economic goals might also no longer reflect reality accurately.

In Sections III and IV, which follow, we confront the socially responsible SWF and consider whether, in fact, it conforms to the spirit of the "deal." In Section V we consider the socially responsible private investment fund as a non-state vehicle for regulatory interventions in private economic markets. Together, they will suggest that the simpleminded formula—formally public and functionally private plus conformity to a model of private non-political behavior equals suitability for regulation like a non-state market participant—may need re-examination.

## III. The Norway Sovereign Wealth Funds

### A. *History*

Norway's SWF is closely tied to the exploitation of petroleum resources within Norway.[110] Petroleum was first discovered in the North Sea in 1969.[111] Oil production started soon thereafter, in 1971. By 1990 a sizeable income from the exploitation of this resource was accumulating and, in response thereto, Norway's Parliament passed

John Ruggie, Voluntary Principles on Security and Human Rights, Remarks at Annual Plenary, Harvard University and United Nations, Washington, D.C 4 (May 7, 2007), *available at* http://198.170.85.29/Ruggie-remarks-Voluntary-Principles-plenary-7-May-2007.pdf.

110. For a history, see, e.g., Martin Skancke, *Fiscal Policy and Petroleum Fund Management in Norway*, *in* Fiscal Policy Formulation and Implementation in Oil-Producing Countries 316, 318-20 (J.M. Davis, R. Ossowski, & A. Fedelino, eds., International Monetary Fund, 2003), *available at* http://www.regjeringen.no/upload/FIN/Statens%20pensjonsfond/Norwegian_petroleum_fund_ms.pdf (last visited Apr. 4, 2009) (the author has been the Director General, Ministry of Finance, Norway).

111. Norwegian Ministry of Fin., Asset Mgmt. Dep't, The Government Pension Fund—Global (Aug. 2008) [hereinafter *Pension Fund Fact Sheet*], http://www.regjeringen.no/upload/FIN/Statens%20pensjonsfond/PF-summary-aug08.pdf.

the Government Petroleum Fund Law.[112] That enactment established the Petroleum Fund as a fiscal policy tool to support a long-term management of the petroleum revenues.[113] It was not invested with separate legal personality, but instead was constituted a department of the government apparatus, to be managed by the Norwegian Central Bank.[114] In 1996 the first net transfer to the Fund was effectuated, which was invested as Central Bank currency reserves. Investment in equities was first introduced in the benchmark with a 40% allocation in 1998.[115]

By 2000 five emerging market countries were added to the equity benchmark. In 2002 non-government bonds were added to the fixed income benchmark. Ethical guidelines for the Fund were issued in 2004 based on the recommendations of a government commission. Such guidelines have two main elements, namely, a) the Fund is an instrument for ensuring that a reasonable portion of Norway's petroleum wealth benefits future generations representing an ethical obligation for present generations to manage it in a way that generates a sound return; b) the Fund does not make investments which constitute an unacceptable risk in which the Fund may contribute to unethical acts or omissions, such as violations of fundamental humanitarian principles, violations of human rights, gross corruption or severe environmental damages.

The Government Petroleum Fund was renamed the Government Pension Fund in 2006. The Fund comprises i) the Government Pension Fund—Global, and ii) the Government Pension Fund—Norway. The

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112. The Act on the Government Petroleum Fund (Act of June 22, 1990, No. 36) (Nor.). *See* Tore Eriksen, *The Norwegian Petroleum Sector and the Government Pension Fund—Global* 7 (2006), *available at* http://www.regjeringen.no/upload/FIN/Statens%20pensjonsfond/The_Norwegian_Petroleum_Sector_te.pdf (the author was then Secretary General, Ministry of Finance, Norway).

113. *See Pension Fund Fact Sheet*, *supra* note 111. "Long term management of petroleum wealth reflects a fundamental social perspective, and is an overarching priority for the Government. Such management implies that this wealth can benefit all generations. At the same time, it makes an important contribution to stability in output and employment. These are necessary prerequisites for realizing the vision of a qualitatively better society." Norwegian Ministry of Finance, *Report No. 24 (2006-2007) to the Storting, On the Management of the Government Pension Fund in 2006*, at 5, *available at* http://www.regjeringen.no/pages/1966215/PDFS/STM200620070024000EN_PDFS.pdf. (last visited Dec. 17, 2009) [hereinafter *Report No. 24*].

114. *See* NORWEGIAN MINISTRY OF FIN., ASSET MGMT. DEP'T, The Management of the Government Pension Fund—Global, http://www.regjeringen.no/en/dep/fin/Selected-topics/The-Government-Pension-Fund/The-Management-Model.html?id=429362 (last visited March 30, 2009) [hereinafter *Management of the Government Pension Fund*].

115. *Pension Fund Fact Sheet*, *supra* note 111. The delay was caused by large budget deficits in the first half of the 1990s. Eriksen, *supra* note 112, at 7.

foreign portion is deposited in an account at Norges Bank, and managed under further rules established by Norway's Ministry of Finance. The domestic portion is placed as a capital contribution to Folketrygdfondet, and managed under further rules also established by Norway's Ministry of Finance.[116] In 2007, strategic equity allocation for the Government Pension Fund—Global (GPF) was increased to 60% and small-cap stocks were included in the benchmark. As of 2008, the GPF's plan was to invest up to 5% in real estate over time from the bond allocation, and to include all emerging countries in the equity benchmark.[117] Norway's Sovereign Wealth fund has been characterized as a model for sovereign wealth funds and its characteristics are considered best practices by international standards.[118] But, reflecting that amalgamation of private and public governance frameworks, the aims of management "for international best practice, and the exercise of ownership rights is based on internationally accepted principles such as the UN Global Compact and the OECD Guidelines of Corporate Governance and for Multinational Enterprises."[119]

One of the most distinguishing, and lauded,[120] features of the GPF is its transparency.[121] The International Monetary Fund indicates that Norway's "Ministry of Finance reports regularly on the governance framework, the fund's goals, investment strategy and results, and ethical guidelines. The Central Bank—the fund's operational manager- publishes quarterly and annual reports on the management of the fund, including its performance and an annual listing of all investments. Detailed information on the fund's voting in sharehold-

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116. NORWEGIAN MINISTRY OF FIN., ASSET MGMT. DEP'T, Provisions on the Management of the Government Pension Fund, http://www.regjeringen.no/en/dep/fin/Selected-topics/The-Government-Pension-Fund/the-guidelines-for-the-management-of-the.html?id=434605 (last visited Nov. 20, 2009) [hereinafter *Pension Fund Management Provisions*].

117. *Pension Fund Fact Sheet, supra* note 111.

118. "In relation to the current debate on SWF, the management of the Government Pension Fund- Global is often cited as an example to be followed." NORWEGIAN MINISTRY OF FIN., ASSET MGMT. DEP'T, Norway's Position in the Debate on Sovereign Wealth Funds, (2007) http://www.eu-norway.org/NR/rdonlyres/2271B78B2D264E399421B2CA3C3DFDC4/80129/NorwayposSWF.pdf (last visited April 3, 2009) [hereinafter *Norway's Position on Sovereign Wealth Funds*].

119. *Id.*

120. An article by Kavaljit Singh published by the Centre for Research on Globalization indicates that "there are very few non-SWFs and institutional investors that can match up to the high standards of transparency, governance and accountability of the Norwegian SWF." Kavalijt, Singh, *"Sovereign Wealth Funds" Towards a Structural Shift in World Financial Order*, THE ECONOMIC TIMES, Nov. 11, 2008, *available at* http://www.globalresearch.ca/index.php?context=va&aid=10904 (last visited Dec. 18, 2009).

121. *Norway's Position on Sovereign Wealth Funds, supra* note 118.

er's meetings is also published."[122]

Additionally, the Fund is only invested abroad in financial assets. The Fund managers suggest that this better ensures risk diversification, financial returns, and reduces the risk of bad governance.[123] According to Norway's official site in the United States, the GPF does not seek to control companies through buy-outs, but "by its own rules the fund restricts its ownership in any company it invests in to five percent of shares. The investment objectives are purely financial in nature, safeguarding assets for the long term."[124]

### B. *Legal Structure*

The framework for the Global Fund was established by the Government Pension Fund Act, which, as amended, remains the legal basis for the fund.[125] Under the Pension Fund Act, the Ministry of Finance is the formal owner of the Fund. However, all significant changes to the Fund's investment strategy are in practice presented to Parliament before implementation as a way of ensuring broad political support for important strategic choices."[126] Administration of the Fund is divided into three parts. The first involves establishing overall policy. This function remains in the Ministry of Finance. The second vests control over management to the Norwegian Central Bank. Lastly, ethical issues involved in the application of the investment strategy by the Central Bank though its management apparatus is to be overseen by an autonomous ethics council. Each is discussed in turn.

The Storting (The Norweigan Parliament) established an advisory Council on investment strategy in 2005 to assist the Ministry of Finance in establishing the guidelines within which the SWFs are operated.[127]

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122. Velculescu, *supra* note 7.

123. The overall parameters of such investment are specified by regulation. *See Pension Fund Management Provisions, supra* note 116; *see also* discussion *infra* at Part III.C.

124. Arild Strømmen, *Transparency and Trust: Keys to the Norwegian Pension Fund,* Royal Norwegian Embassy, Washington, D.C., http://www.norway.org/ARCHIVE/policy/gpf/norwegian_pension_fund_global (last visited Nov. 21, 2009).

125. *See Pension Fund Management Provisions, supra* note 116.

126. *Foreign Government Investment in the U.S. Economy and Financial Sector*: Hearing *Before The Subcomm. on Domestic and Int'l Monetary Policy, Trade & Tech., & the Subcomm. on Capital Mkts., Insurance, and Gov't Sponsored Enterprises* (2008) (statement of Martin Skancke, Director General, Asset Management Department, Norwegian Ministry of Finance) [hereinafter *Skancke Statement*].

127. The Ministry of Finance, Norway, The Investment Strategy Council, *available at* http://www.regjeringen.no/en/dep/fin/Selected-topics/The-Government-Pension-Fund/The-Investment-Stategy-Council.html?id=434880 (last visited Apr. 4, 2009). The Council was established on September 29th 2005. *Id.* "The Government Pension Fund Bill, no. 2 (2005–2006), states that the

"The Ministry of Finance's Advisory Council on Investment Strategy (Investment Strategy Council) will assist the ministry in the latter's work on the long-term, overarching investment strategy for the Petroleum Fund. Key investment strategy issues are the choice of weights for geographical regions and asset classes and the inclusion of new investment alternatives."[128] The role of the Investment Strategy Council is essentially passive.[129] While it makes recommendations, the power to make decisions remains with the Ministry of Finance. But even the Investment Strategy Council's discretion with respect to the recommendations it may offer is limited by the objectives of the set of "overarching principles"[130] that suggest purely private investment objectives.[131] Thus, in this respect, the Fund complies with the ethos—formally public and functionally private model.

That model is further deepened by the form of the organization of the management of the Norwegian Global Fund. The Government Pension Fund Act of 2005 governs the establishment and operation of the management of the Global Fund.[132] The Ministry of Finance has delegated responsibility for the operational management of the Global Fund to Norges Bank.[133] The Fund itself is represented by an account held by the Norges Bank in the name of the Ministry of Finance. The

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advisory council will continue as advisor to the Government Pension Fund—Global." *Id.* The Council has no legal personality. "The Ministry of Finance will be the contractual counterparty in any agreements that the council needs to enter into with other parties." *Id.*

128. *Id.*

129. "The council will at the outset consider matters put to it by the Ministry of Finance. The council will on a regular basis be asked to review issues related to the long-term investment strategy. The council will be entitled to address issues on its own initiative." *Id.*

130. *Id.* These include the achievement of a high return subject to moderate risk, investment only in foreign instruments, the use of the fund as "a financial investor and not [as] a tool for strategic ownership of individual companies," diversification, and the application of a long-term investment horizon. *Id.*

131. However, these limits are not extended to management issues, which are addressed to other administrative bodies. "The council shall not make recommendations regarding the organisation of the management regime. The Ministry of Finance has delegated the operative management, including selection of external managers, to Norges Bank." *Id.* Likewise, ethics issues are also addressed elsewhere. "The Ministry of Finance's Advisory Council on Investment Strategy shall not give advice regarding the Petroleum Fund's ethical obligations. It is the responsibility of the Petroleum Fund's Advisory Council on Ethics to consider whether investments in individual companies are contrary to the Petroleum Fund's ethical guidelines." *Id.*

132. *Pension Fund Management Provisions*, *supra* note 116.

133. "The Government Pension Fund Act assigns the management of the Fund to the Ministry of Finance. The operational management of the Government Pension Fund—Global is carried out by Norges Bank while the Government Pension Fund—Norway is handled by Folketrygdfondet." *Management of the Government Pension Fund*, *supra* note 114.

value of the account is the amount that may be invested by the investment arm of the bank.[134] The income of the Global Fund is the cash flow from petroleum activities, which is transferred from Norway's central government budget, the return on the GPF capital, and the net results of financial transactions associated with petroleum activities.[135]

According to a Finance Ministry official, the Government Petroleum Fund Act of 1990 stated that the Fund's capital was to be invested in the same way as the government's other assets, thus it seemed logical that the operational management of the GPF be carried out by Norges Bank,[136] which invests the fund's capital in bonds and equities outside of Norway in accordance with guidelines issued by Norway's Ministry of Finance.[137] The relationship between Norway's Ministry of Finance and Norges Bank is governed by a Management Agreement. Norway's Ministry of Finance has adopted regulations on the Global Fund, and it sets guidelines, including benchmark and risk limits, and exercises oversight. In addition, a Supervisory Council, reporting directly to the Storting, supervises Norges Bank's activities.[138] "Underlying these objectives is an acknowledgement that Norges Bank manages substantial assets on behalf of Norwegian society."[139]

Norges Bank's management established the Norges Bank Investment Management (NBIM) on January 1, 1998 as an operational investment

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134. *See Skancke Statement*, *supra* note 126, at 3-4 ("The value of the Ministry's account in the Bank is set equal to the market value of the corresponding pool of foreign assets held by the Bank. The Ministry therefore bears the risk of changes in the market value of the assets."). The sources of assets are identified by statute. *See Pension Fund Management Provisions*, *supra* note 116.

135. *Pension Fund Management Provisions*, *supra* note 116.

136. Strømmen, *supra* note 122.

137. Norway Ministry of Finance, *The Government Pension Fund*, *available at* http://www.regjeringen.no/en/dep/fin/Selected-topics/The-Government-Pension-Fund.html?id=1441 (last visited Dec. 16, 2009).

138. Norwegian Ministry of Finance, *Report No. 16 (2007-2008) to the Sorting on the Management of the Government Pension Fund in 2007*, at 139, *available at* http://www.regjeringen.no/pages/2064594/PDFS/STM200720080016000EN_PDFS.pdf [hereinafter *Report No. 16*] (quoting report of it auditors). It is composed of fifteen members, all elected by the Storting. Its responsibilities include formal approval of the Bank's financial statements, adoption of the Bank's budget arrangements for the hiring of and the instructions to the Central Bank's auditor, Norges Bank Audit. *Id.*

139. NORGES BANK INVESTMENT MANAGEMENT, GOVERNMENT PENSION FUND-GLOBAL ANNUAL REPORT 2008, at 7, *available at* http://www.norges-bank.no/upload/73979/nbim_annual report08_rev.pdf [hereinafter GOVERNMENT PENSION FUND 2008].

management unit for the management of the Global Fund.[140] In addition, NBIM hires outside managers to direct the investment of sectors of its portfolio.[141] Norway's Ministry of Finance stresses a high degree of openness for purposes of strengthening the confidence in the Global Fund and its structure. Operational management performance is reported by Norges Bank on a regular basis. The Ministry of Finance provides an annual report on the management of the Fund to the Storting during the spring session[142] and such reports are public and widely disseminated in English. "The auditing of the Fund and its management is done by the Office of the Auditor General. The Auditor General is appointed by and reports directly to Parliament, ensuring parliamentary control on [GPF's] operations."[143]

This organizational structure suggests both the formal connection between the state apparatus and the Fund, as well as a significant measure of separation between the effective management of the Fund and the apparatus of state. The organizational structure is meant to make it formally difficult for the state to intervene effectively in only a supervisory capacity without substantial effort. At the same time, it is clear that state intervention is possible, and that state policy marks the outer boundaries of acceptable management. Still, that policy at least formally adheres to the private actor model of investment. The extent of that functional privatization is tested in the formulation of investment principles and the operation of the third leg of the Fund's management—the Ethics Council, topics taken up in the next section.

### C. *Investment Principles*

"What constitutes a good investment strategy for the Government Pension Fund is determined by the characteristics of the Fund, the purpose of the investments, the owners' (the people of Norway, represented by the political authorities) tolerance of risk, and assumptions

140. NORGES BANK INVESTMENT MANAGEMENT, TEN YEARS OF NBIM, *available at* http://www.norges-bank.no/upload/nbim/reports/2007%20feature1.pdf; *See also*, GOVERNMENT PENSION FUND 2008, *supra* note 139, at 8.

141. For example, NBIM employed outside managers for investment in the United States. That proved a costly decision in light of the collapse of Lehman Brothers in 2008. *See id.* at 11.

142. *See generally*, Norwegian Ministry of Finance, *National Budget 2009, Chapter 5, The Management of the Government Pension Fund*, at 2, *available at* http://www.regjeringen.no/pages/2115161/Chapter%205%20National%20Budget%202009.pdf [hereinafter *Chapter 5*].

143. Eriksen, *supra* note 112, at 15.

about how the financial markets work."[144] The Ministry of Finance has taken the position that

> "there is a broad political consensus that the Pension Fund should be managed with a view to achieving the maximum possible return within a moderate level of risk. The Ministry of Finance has formulated a long-term investment strategy ensuring that the capital is invested in a broad-based portfolio comprising securities from many countries. The long investment horizon of the Fund means that the portions invested in various asset classes and geographical regions can be determined on the basis of assessments of expected long-term returns and risks."[145]

Investment principles have been defined by law, through the Regulations on Management of the Government Pension Fund.[146] They mandate that the GPF is placed in a separate account in the form of krone deposits with Norges Bank. Norges Bank invests this capital in its own name in financial instruments and cash deposits denominated in foreign currency.[147] According to the Fact Sheet on the GPF published by the Norwegian Ministry of Finance on August 2008,

> "the average ownership share in listed companies is less than 1%, the upper limit is set at 10%. Equities account for 60% of the fund's strategic benchmark portfolio, consisting of equities listed on exchanges in Europe (50%), America/Africa (35%) and Asia/Oceania (15%). All emerging markets are included, as defined by index provider FTSE. Fixed income instruments account for 35% of the strategic benchmark portfolio, consisting of fixed income instruments issued in currencies from Europe (60%), America/Africa (35%) and Asia/Oceania (5%), while real estate investments take up the remaining 5%."[148]

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144. Norwegian Ministry of Finance, *Report No. 20 (2008-2009) to the Storting, On the Management of the Government Pension Fund in 2008,* at 4-5, *available at* http://www.regjeringen.no/upload/FIN/Statens%20pensjonsfond/stmeld20_2008-2009/report_no20_2009.pdf (last visited Apr. 10, 2009) [hereinafter *Report No. 20*].

145. *Chapter 5, supra* note 142.

146. *Pension Fund Management Provisions, supra* note 116.

147. *Id.*

148. *Pension Fund Fact Sheet, supra* note 111.

The Fund's investment strategy is implemented through a benchmark portfolio.[149] It is based on a set of current consensus notions about the way that markets function.[150]

It is in the application of its investment principles that the Global Fund suggests a deviation, even as a formal matter, away from the idealized model of a private investor and the privileging solely of financial and economic objectives. "The Goal of the Government Pension Fund—Global is to be managed responsibly in a manner that takes good corporate governance and environmental and social issues into account."[151] This suggests a set of political objectives, centered on the need to satisfy the aspirations of the Norwegian people as applied to Norway's conduct abroad—in this case through the use of its private market participation.[152] The object appears to be to blend the public and private within a redefined understanding of politically motivated private conduct.[153]

The most important and controversial aspects of the application of the Global Funds' investment principles are bound up in ethical guidelines for investment.[154] The Guidelines are based on two premises. The first is that the Fund must be managed to protect the wealth generated by the exploitation of Norway's extractive industries, mostly petroleum, and to extract a "sound return in the long term."[155] The second is that the first objective is contingent on a number of policy factors, including "sustainable development in the economic, environmental and social sense."[156] The policy nature of these contingencies is clearly articulated as well. The Fund is to be used not merely to protect and increase the value of the Fund itself, but to influence behaviors

149. *Report No. 20*, *supra* note 144, at 5, 9-16.

150. *Id.* at 7 (efficiency, diversification across market segments, and among investment instruments).

151. *Id.* at 5.

152. *Id.* ("The Government requires that responsible management of the Fund is arranged in such a way that support is ensured among the population of Norway and legitimacy among market players.")

153. *Id.* at 6. ("One goal in the role as a responsible investor is to promote sustainable development in economic, ecological and social terms, this is regarded as a precondition for good financial returns over time." "This is in keeping with the United Nations' Principles for Responsible Investments.")

154. Styrer, Rad Og Utvalg, Ethical Guidelines, Norwegian Government Pension Fund—Global, *available at* http://www.regjeringen.no/en/sub/Styrer-rad-utvalg/ethics_council/ethical-guidelines.html?id=425277 (last visited Mar. 25, 2009).

155. *Id.* at Clause 1.

156. *Id.*

among the pool of potential targets of investment. First, the Fund is to have a proactive policy charge: "The financial interests of the Fund shall be strengthened by using the Fund's ownership interests to promote such sustainable development."[157] And second, the Fund is to to avoid investment in companies it deems might "contribute to unethical acts or omissions, such as violations of fundamental humanitarian principles, serious violations of human rights, gross corruption or severe environmental damages."[158]

To meet its objectives, the Ethical Guidelines provide recommendations on the Fund's implementation.[159] It is grounded on three principal activities—exercise of ownership rights, negative screening of companies, and exclusion of companies from the investment pool.[160] The exercise of shareholder rights[161] is grounded in the web of soft law behavior rules that have been emerging from the work of the Organization for Economic Cooperation and Development (OECD),[162] and the United Nations.[163] Both of these organs have produced a set of voluntary codes that are exerting increasing influence on the ways in which appropriate corporate behavior is judged.[164] Negative screening is meant to form the basis for implementing the ethics objective to avoid investment in companies "that either themselves, or through entities they control, produce weapons that through normal use may violate fundamental humanitarian principles."[165] Screening serves as the basis for exclusion. The obligation to exclude is triggered where there is a finding of unacceptable risk of contributing to a list of

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157. *Id.*

158. *Id.* at Clause 2.

159. *Id.*

160. *Id.*

161. *Id.* ("Exercise of ownership rights in order to promote long-term financial returns, based on the UN Global Compact and the OECD Guidelines for Corporate Governance and for Multinational Enterprises.").

162. *See, e.g.*, OECD PRINCIPLES OF CORPORATE GOVERNANCE (2004), *available at* http://www.oecd.org/dataoecd/32/18/31557724.pdf (last visited Feb. 28, 2009); OECD Guidelines for Multinational Enterprises, *supra* note 35.

163. *See* U.N. GLOBAL COMPACT (UNGC), OVERVIEW OF THE U.N. GLOBAL COMPACT, *available at* http://www.unglobalcompact.org/AbouttheGC/index.html (last visited Feb. 11, 2009) ("The UN Global Compact is a strategic policy initiative for businesses that are committed to aligning their operations and strategies with ten universally accepted principles in the areas of human rights, labour, environment and anti-corruption."). On the genesis of the UNGC, *see* ANDREW CLAPHAM, HUMAN RIGHTS OBLIGATIONS OF NON-STATE ACTORS 218-25 (Oxford Univ. Press, 2006).

164. For a discussion see Backer, *Rights and Accountability*, *supra* note 36.

165. Styrer, Rad Og Utvalg, *supra* note 154, at Clause 2.

undesirable activities.[166] In this way the mechanics can be understood as based on adherence to a set of behavioral norms generated by two international and transnational actors, an obligation to screen investment targets on the basis of those norm frameworks, and an obligation to exclude companies from investment that fail to adhere to those norms, but only with respect to a specified list of conduct breaches and only when adjudged to meet the severity standards of the Fund.

The Ethics Guidelines' focus on the exercise of ownership rights suggests a role for shareholder activism that is further elaborated in the Guidelines.[167] It, like the ethical objectives, appears to suggest a hybrid model. On the one hand, the Fund's objective as a shareholder is the conventional one—"to safeguard the Fund's financial interests."[168] But those shareholder efforts are tied not merely to maximize shareholder wealth, but also to further the normative objectives of corporate social responsibility enshrined in the United Nation's Global Compact and the OECD Guidelines for Corporate Governance and the Guidelines for Multinational Enterprises.[169] Those obligations are to be exercised by Norges Bank and reported annually.[170] The Bank, however, is permitted to delegate the exercise of ownership rights to external managers, as long as those managers are themselves bound by the Ethical Guidelines.[171]

Negative screening and exclusion provide the heart of the operationalization of the Ethics Guidelines, for which an institutional framework and procedures are established, and lines of authority delineated.[172] The Ethics Guidelines are overseen by a Council of Ethics, established by Royal decree in 2004 and revised in 2005.[173] The Ethics Council consists of five members[174] and is entitled to some support.[175] The

166. These activities include: (1) Serious or systematic human rights violations, such as murder, torture, deprivation of liberty, forced labour, the worst forms of child labour and other child exploitation; (2) serious violations of individuals' rights in situations of war and conflict; (3) severe environmental damage; (4) gross corruption; and (5) other particularly serious violations of fundamental ethical norms. *Id.*

167. *Id.* at Clause 3.

168. *Id.* at Clause 3.1.

169. *Id.*

170. *Id.* at Clause 3.2.

171. *Id.* at Clause 3.3.

172. *Id.* at Clause 4.

173. *Id.*

174. *Id.* at Clause 4.2 ("The Council on Ethics for the Government Pension Fund – Global shall consist of five members. The Council shall have its own secretariat."). The current Council members are Professor Ph.D. Andreas Føllesdal, Associate Professor Dr. Juris Gro Nystuen (Chair

Ethics Council is constituted as an independent advisory body, the principle objective of which is to assess whether particular companies ought to be excluded from investment by the Government Pension Fund—Global and to submit its recommendations with respect thereto to the Minister of Finance.[176] These recommendations are made upon request of the Finance Ministry.[177] The Ministry of Finance makes decisions on the exclusion of companies from the Fund's "investment universe" based on the Council's recommendations. Both the Ministry's decisions and the Council's recommendations will be made publicly available on [a] website."[178] But the Ministry of Finance is permitted to delay reporting where such delay "is deemed necessary in order to ensure a financially sound implementation of the exclusion of the company concerned."[179] Exclusion recommendations are reserved for companies with respect to which the Ethics Council determines that their acts or commissions constitute an unacceptable risk to the Fund of contributing to human rights violations, the rights of individuals in conflict zones, severe environmental damage, gross corruption, or "other particularly serious violations of fundamental ethical norms."[180]

The Ethics Council is required to make a recommendation of exclusion after the conduct of a negative screening investigation where the Council concludes that the companies at issue either "produce weapons that through their normal use violate fundamental humanitarian principles; or sell weapons or military materiel to states."[181] The recommendation in turn is based on two conclusions. The first is that

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of the Council), Director Corporate Finance and Managing Director Bjørn Østbø, Programme Manager Anne Lill Gade, and Professor Ola Mestad. Styrer, Rad Og Utvalg, *Council of Ethics, Norwegian Government Pension Fund—Global,* http://www.regjeringen.no/en/sub/Styrer-rad-utvalg/ethics_council.html?id=434879 (last visited Nov. 13, 2009) [hereinafter *Ethics Council*].

175. The Council is supported by a secretariat. According to its 2007 Annual Report, that Secretariat consisted of six employees—an economist, an individual with a master's degree in law and several candidates for higher degrees. SEE COUNCIL ON ETHICS GOV'T PENSION FUND—GLOBAL, ANNUAL REPORT 2007, 7 (2007), *available at* http://www.regjeringen.no/pages/1957930/Annual%20Report%202007.pdf (last visited March 25, 2009) [hereinafter *Annual Report 2007*].

176. *Id.* at 4.

177. Styrer, Rad Og Utvalg, *supra* note 154, at Clause 4.3

178. *Ethics Council*, *supra* note 174 ("The role of the Council on Ethics for the Government Pension Fund—Global is to provide evaluation on whether or not investment in specified companies is inconsistent with the established ethical guidelines."); *see also* Styrer, Rad Og Utvalg, *supra* note 154, at Clause 4.1.

179. *Id.*

180. *Id.* at Clause 4.4.

181. *Id.* The states against which weapons sales are interdicted are set forth "in Clause 3.2 of the supplementary guidelines for the management of the Fund." *Id.*

there is a connection between the company under investigation and the ethical violation described in the Ethics Guidelines. The second is that the connection between company and violation in turn represents an unacceptable risk for the company (and the Fund) to contribute to future violations.[182]

A critical portion of the intake investigative work of the Council of Ethics is privatized. It "receives a monthly report regarding companies that are accused of environmental damage, human rights violations, corruption or other contraventions. The service is provided by an information supplier, who conducts daily news searches on all companies within the Fund's portfolio."[183] Beyond that, much of the Council's investigation is meant to be undertaken through Norges Bank.[184] Process rights of an elementary sort are also included in the Ethics Guidelines.[185] The principal one requires that companies threatened with exclusion be given a draft of the recommendation, the reasons supporting it and an opportunity to comment.[186] Excluded companies are also to be informed of decisions to that effect by the Finance

182. *See* MINISTRY OF FINANCE, *The Report from the Graver Committee* (Nov. 7, 2003), http://www.regjeringen.no/en/dep/fin/Selected-topics/andre/Ethical-Guidelines-for-the-Government-Pension-Fund–Global-/The-Graver-Committee–documents/Report-on-ethical-guidelines.html?id=420232&epslanguage=EN-GB (last visited Mar. 24, 2009).

183. *Annual Report 2007*, *supra* note 175, at 4.

184. Styrer, Rad Og Utvalg, *supra* note 154, at Clause 4.5. "The Council may request Norges Bank to provide information as to how specific companies are dealt with in the exercise of ownership rights. Enquiries to such companies shall be channelled through Norges Bank. If the Council is considering recommending exclusion of a company, the company in question shall receive the draft recommendation and the reasons for it, for comment." *Id.*

185. *Id.*

186. Simon Chesterman has explained:

> Technically it is not a legal tribunal bound by rules of due process; technically it focuses on the risk of complicity on the part of the fund rather than proof of allegations against a given company. In practice, however, it has justified its decisions on quasi-legal grounds, establishing precedent and following or distinguishing prior decisions; it has also adopted a quasi-adversarial procedure, allowing companies the opportunity to know allegations and respond to them, though without the full trappings of legal process.

Simon Chesterman, Norge Finansdepartementet, *Laws, Standards or Voluntary Guidelines?* (Dec. 20, 2007) http://www.regjeringen.no/nb/dep/fin/Kampanjer/Investing-for-the-Future/LAWS-STANDARDS-OR-VOLUNTARY-GUIDELINES.html?id=495027, (last visited March 24, 2009); *see generally* Simon Chesterman, *Oil and Water: Regulating the Behavior of Multinational Corporations Through Law*, 36 N.Y.U. J. INT'L L. & POL. 307 (2004).

Ministry.[187] Yet exclusion does not end the investigative work. The Council is required to review exclusions on a regular basis and to recommend reinstatement where appropriate in light of new information.[188] The notion suggests that exclusion is not merely a business decision, but an effort to create incentives for change in the behavior of the companies affected.

The Ethics Council is well aware of its role in the global discussion of corporate governance, and global efforts to regulate transnational corporate activity. "Our experience shows that there is a keen interest in our activities, both in Norway and abroad. The contact with various research institutions, non-governmental organisations, and media representatives are important to our work, and we look forward to valuable suggestions and opinions also in 2008."[189] The Funds have published studies that go to the utility of the use of Sovereign Wealth Funds to assume a critical role in the governance of multinational corporations.[190] During the first year of its operation, the Council focused on exclusion of companies involved in the munitions business.[191] It has since moved on to other significant issues touching on the most current global governance and regulatory issues in transnational business regulation, assessing eighty companies in 2007.[192] It is to those that the article turns to next.[193]

## IV. THE NORWAY FUNDS IN ACTION: PRIVATE AND PARTICIPATORY OR PUBLIC AND REGULATORY?

The formal organization of the Norwegian SWF produces a curious tension. It is constructed for the most part to achieve the aim of establishing a substantially autonomous investment unit, that operates free of political pressure. Yet its organization also introduces a political

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187. *See* Styrer, Rad Og Utvalg, *supra* note 184, at Clause 4.7 ("The Ministry of Finance may request that Norges Bank inform the companies concerned of the decisions taken by the Ministry and the reasons for the decision.").

188. *Id.* at Clause 4.6.

189. Council on Ethics for the Gov't Fund—Global, *Annual Report 2006*, 5 (2007), *available at* http://www.regjeringen.no/upload/FIN/etikk/etikk_06_annual%20report.pdf [hereinafter *Annual Report 2006*].

190. *See* Chesterman, *supra* note 186.

191. *Annual Report 2006*, *supra* note 189. That focus continued thereafter; *see also*, *Annual Report 2007*, *supra* note 175, at 5 ("During the year, the Council has initiated monitoring of the new benchmark portfolio in order to identify companies that produce weapons which should be screened out of the Fund.").

192. *See Annual Report 2007*, *supra* note 175, at 4.

193. *See* discussion *infra* Section IV.

element into the heart of the formal organization of the management of the Global Fund, particularly in the form of the Ethics Council. This produces a certain ambiguity in Fund behavior—it operates like a private investment fund to the extent that it seeks to maximize shareholder value, but the maximization of shareholder value in this case requires the Fund be used to effect the global governance goals of the Norwegian state, an analysis to which the article turns to last.[194] That ambiguity is nicely evidenced in the way in which investment policy is driven by notions of corporate social responsibility and in the way in which the Global Fund has responded to the financial crisis of 2008. Each is discussed in turn.

### A. *Corporate Social Responsibility and Ethics*

The formal organization of the Norwegian SWF, in both its internal and external aspects thus suggests an organization that mimics, to a substantial extent, the practices of private investment vehicles. The underlying objectives of the funds are economic or commercial—value maximization of fund assets over some certain time horizon. Yet the activities of the funds in practice suggest an interesting twist on the application of these norm frameworks. I will briefly look at three applications of this investment policy: (1) corporate social responsibility; (2) sanctions against Israel; and (3) investment in Burma. The three suggest the way in which public and private interest may merge, and the way in which, as some critics fear,.public policy can be deployed within markets.

#### 1. Corporate Social Responsibility

Corporate social responsibility, in the form of exercising shareholder rights, is an important element of the investment strategy of the Norwegian Funds.[195] The Fund management has focused on a few

194. *Id.*

195. The Fund reported its conception of that responsibility quite directly:

> investors should also share responsibility for how the companies in which they invest are conducting themselves, for what they are producing and for how they are treating the environment. The Government deems it important to integrate this type of responsibility into the management of the Government Pension Fund, because it promotes values that are important to the Norwegian people, and because it represents an important contribution to raising awareness amongst investors and companies domestically and abroad.

specific areas of corporate governance, which it has raised with entities whose equities they hold (as well as with the governments that have chartered those entities).[196] For this purpose, the Bank has identified three broad areas of shareholder activism: corporate governance, children's rights and environmental protection.[197] Corporate governance is the gateway to issues of social and environmental activism.[198] With respect to corporate governance, the Global Fund asserted shareholder power in two ways—by voting and through direct communications with companies.[199] With respect to children's rights, NBIM has produced a set of guidelines that describe its investor expectations "for corporate performance with regard to preventing child labour and promoting children's rights."[200] The object is not merely to serve as a guideline for Global Fund investment, but to influence the behavior of other investors (and thereby pressure entities to conform to the expectations).[201] The efforts, though, are framed in financial and economic terms.[202] The Norges Bank environmental investor policy is particularly interesting for its conformity to an idealized private investor model. That policy is grounded on the idea that it, as an investor

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Report No. 24, *supra* note 113, ¶ 4.1.1 (integration of ethical considerations in the management of the Government Pension Fund).

196. *Report No. 20*, *supra* note 144, at 16 ("Norges Bank bases its exercise of the ownership rights of the Fund on the belief that it is better and more effective to concentrate on a few important topics than to spread the resources thinly over many areas.").

197. *Id.*

198. *Id.* at 17.

199. *Id.* ("At the end of 2008, Norges Bank had established or continued dialog with 16 companies concerning issues linked to corporate governance and shareholder rights.... In 2008, Norges Bank took part in 7,871 general assemblies and voted on almost 70,000 issues . . . [and] voted against 11 percent of the proposals.").

200. NORGES BANK INVESTMENT MANAGEMENT, NBIM INVESTOR EXPECTATIONS ON CHILDREN'S RIGHTS, at 3, *available at* http://www.norges-bank.no/upload/nbim/cg/expectations%20childrens%20rights.pdf. The expectations include the development of a conforming corporate child labor policy, continuous risk assessment, preventive and corrective plans and actions, supply chain management systems, monitoring systems, performance reporting, integration of potential economic impacts of social issues into corporate strategic planning and a transparent and well-functioning corporate governance system. *Id.* at 12.

201. "The NBIM Investor Expectations on Children's Rights will serve as a reference for investors who adhere to the principles of responsible investment, and can be used as an indicator of best business practices by corporations globally. The primary function of the Expectations is not to blacklist or rank companies, but to serve as a point of departure for constructive dialogue between investors and companies, and to set a clear standard that companies globally must be expected to live up to." *Id.* at 4.

202. *Id.* at 4-5.

must "influence how companies work with or against government authorities when it comes to establishing binding climate legislation that can result in significant reductions in greenhouse gases."[203]

In addition, Norges Bank has begun to work in concert with other funds, both public and private, to effect changes in the ways that governments approach environmental issues.[204] The Bank also works on global legislative issues that affect corporate behavior, including accounting standards for companies in extractive industries, and the development of the United Nations Principles for Responsible Investing.[205] This suggests two things. First, it suggests that the Global Fund does not adhere strictly to the ideal private investor model of the formally public/functionally private framework. Second, it appears that private funds do not limit their activities to financial and economic welfare maximization either.

Moreover, it is in the area of shareholder rights that sovereign wealth fund governance and the governance of multinational corporations meet. "The principles governing the exercise of the ownership rights of the Government Pension Fund are based on the UN Global Compact, the OECD Principles of Corporate Governance and the OECD Guidelines for Multinational Enterprises."[206] These soft law frameworks serve as the basis of the more pointed shareholder action program developed by the Fund. "Norges Bank and Folketrygdfondet have, on the basis of these principles, defined their own principles governing the exercise of the ownership rights of the Government Pension Fund—Global and the Government Pension Fund—Norway, respectively."[207] These include three principal areas of governance:

> good corporate management, with a main emphasis on owners' rights to nominate and appoint directors, to exercise their voting rights, to trade in their equities and to exercise influence over anti-takeover mechanisms, and to receive transparent and timely information; children's rights and health, hereunder the battle against child labour, with a main emphasis on the value chains of multi-national companies; and corporate lobbying in

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203. *Report No. 20, supra* note 144, at 17.

204. "In November 2008, Norges Bank announced that the bank was taking part in a new petition by 135 funds calling for wealthy nations to reduce their emission of greenhouse gases." *Id.*

205. *Id.* at 18.

206. *Report No. 16, supra* note 138, at 117.

207. *Id.*

relation to long-term environmental problems, hereunder climate changes.[208]

The wide-ranging and international focus of Fund investing reflects what the Norges Bank sees as an international consensus on public and private activity within markets. That consensus rejects the distinctions between public and private activity. It focuses, instead, on a functional approach in which both public and private actors are burdened with regulatory and policy obligations.[209]

The corporate governance agenda of the Global Fund suggests both the private and public side of Norway's investment strategy. The Funds use traditional methods of asserting shareholder power with respect to their substantive and ethical agendas. These include voting, dialog with companies, cooperation with other shareholders, and external communications (with public and civil society actors). With respect to issues of shareholder activism, the Fund does not necessarily pursue the same forms of action as might be available to a private shareholder. Instead, the Fund focuses on state-to-state dialog, in an attempt to obtain legal reform for targeted corporate governance issues.[210] A more traditional approach, however, was applied with respect to issues of executive compensation.[211] In all cases, the Fund has become far more active

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208. *Id.* at 118-119.

209. *Report No. 20, supra* note 144, at 21 ("To maintain the Fund's solid position as a responsible investor, the Ministry proposes that good corporate governance and environmental and social factors shall be integrated to a greater degree as relevant factors in the overall work on management of the Fund. This is in line with international developments and will entail a raised ambition level in this area.").

210. *Report No. 16, supra* note 138, at 117, at 119. "Norges Bank has, together with other large European investors, pursued a dialogue, through meetings and letter, with the Chairman and members of the U.S. Securities and Exchange Commission ('SEC'), concerning the importance of establishing regulations that ensure the shareholders real influence over the appointment of directors of US companies. The Bank deems progress thus far to be inadequate, and will continue to follow up on this issue in 2008."

211. The Report to Parliament explained:

> Norges Bank voted against the proposals recommended by management in 25 pct. of the cases relating to remuneration. The Bank did not support the approval of remuneration plans that were not linked to actual performance, that permitted the repricing of options, that resulted in a relatively high degree of dilution of the ownership stakes of existing owners, and that were allotted at a price much lower than the market price, or that involved exaggerated pension schemes, as well as pension bonuses for Directors and auditors. Norges Bank also voted against a number of remuneration plans as the result of inadequate information.

with respect to its holdings. The object is to ensure that all companies in which the Fund invests adheres to the Fund's ideas of appropriate corporate governance, irrespective of the national law of the home state.[212] "Work on integrating issues related to corporate governance, the environment and social factors is accordingly important to safeguard the financial interests of the Fund."[213] Where such national law is incompatible with that more to the taste of the Fund, then the Fund works either to change that legal basis,[214] or to work around it to the extent that the statutes permit deviation.[215]

### 2. Israel Boycott

Various combatants in the Israel Palestine conflict and their friends and allies in Europe, in general, and Norway, in particular, have made effective use of the Ethics Guidelines to put financial and media pressure on Israeli companies. The result has been to open another front in that complex war within global financial markets in general and Norway's Funds in particular. The most recent genesis of this strategy has been repeated efforts to seek to exclude Israeli companies and companies that do business in Israel from the investment portfolios of the Norway Funds. "The Norwegian government has responded to Israel's military offensive in the Gaza strip by asking the Council of Ethics, which advises the country's €267bn Government Pension Fund, to check that companies in which it invests in the region are not involved in human or labour rights abuses."[216]

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*Id.*

212. "By virtue of our long-term investments in very many of the world's companies, we have a responsibility for and an interest in promoting good corporate governance and safeguarding environmental and social concerns. The Government will therefore give priority to being a responsible investor in its management of the fund." *Report No. 20, supra* note 144, at 11. "It follows from the task of manager of the public's funds that widely shared ethical values must be taken into account." *Id.* at 12. As such, to "meet these goals, the Ministry wants to integrate the goals of good corporate governance and consideration of environmental and social aspects into all parts of the management." *Id.* at 13. Yet, the Fund insists that there is a difference between this objective and the political objectives of the Norwegian state, at least as to tactics. *Id.*

213. *Id.* at 45.

214. *See Skancke Statement, supra* note 126, at 7.

215. "At the end of 2008, Norges Bank had established or continued dialogue with 16 companies concerning issues linked to corporate governance and shareholder rights." *Report No. 20, supra* note 144, at 20.

216. Hugh Wheelan, *Norwegian Govt Fund Checks Companies for Israel Gaza Human Rights Abuses,* CUPE ONTARIO, Jan. 8, 2009, http://www.cupe.on.ca/doc.php?document_id=

While the determination to check those companies has not produced a blanket recommendation to exclude investment in any class of companies, the Ethics Counsel had begun to report conclusions with respect to individual companies before the announcement of the post-Gaza incursion of 2008-2009 by Israeli forces. The Ethics Committee consideration of a complaint against the Israel Electric Corporation (IEC) by the Norwegian NGO, People's Aid, and a "local group", *Palestinavenner* ("Friends of Palestine").[217] These philo-Palestinian cause entities in Norway alleged that "IEC has reduced the supply of electricity to Gaza and that this amounts to a form of collective punishment of the civilian population in Gaza."[218] IEC, substantially wholly owned by the State of Israel, supplied about 60% of electricity to the Gaza territory.[219] During the autumn of 2007, IEC, under instructions from the Israeli Defense Ministry, reduced electricity supplies to Gaza as part of an economic blockage in response to indiscriminate rocket attacks from the military and civilian population of Gaza.[220] The Ethics Commission considered two actions of public organizations. The first was a report of the United Nations Office for Coordination of Humanitarian Affairs.[221] The assumptions in the report were taken seriously by the

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729&lang=en. (last visited Dec. 16, 2009). "During 2008, the Israel equity market was included for the first time in the Norwegian fund's benchmark meaning that it has invested in a growing number of Israeli companies. Between 2006 and 2008, the Norwegian Council on Ethics on various occasions considered possible contribution to human rights violations or other ethical norms through investment in Israeli companies." *Id.*

217. *See* Letter from Council on Ethics, Norwegian Government Pension Fund—Global, to Ministry of Finance (Apr. 18, 2008), *available at* http://www.regjeringen.no/en/sub/Styrer-rad-utvalg/ethics_council/Recommendations/Other-documents/letter-dated-april-18-2008-on-the-counci.html?id=524431. The Norwegian People's Aid provided information of the humanitarian situation in Gaza and the privations suffered by its population. It could not, however, conform the continuation of power supply restrictions. "Here, it was stated that based on their own enquiries, Norwegian People's Aid could still not determine that the reduction in supply of electricity had actually ceased, but that it was difficult to bring certainty to this question." *Id.* at 3.

218. *Id.*

219. *Id.* at 1. The remainder is provided by Egypt and by a power plant in Gaza. *Id.*

220. *Id.* at 2. The reduction, in the amount of 0.5 megawatts, was confirmed by the U.N. Office for the Coordination of Humanitarian Affairs, focused on the Gazan side of the dispute, pursuant to its report of February 8, 2008, and considered by the Ethics Committee. *Id.*

221. The Report painted a grim picture for the Palestinian population of Gaza and assumed "that there has been a plan to reduce the electricity supply to Gaza as a response to rocket attacks on Israel, and that a reduction by 0.5 MW has been implemented. The report is also understood to suggest that there is an escalation plan which involves further, weekly reductions by 0.5 MW per week." *Id.*

Committee.[222] The second was a discussion of a decision by the Israeli Supreme Court with respect to the legality of the electricity reductions by IEC.[223] "This, however, has no direct bearing on the Council's assessment."[224] In addition, the Ethics Committee heard from the Israeli Ambassador to Norway[225] and from Palestinian official sources.[226]

On the basis of this information, the Ethics Council first acknowledged that its forum was being used as a site for the continuation of the conflict between the Israelis and Palestinians, but that it "is the role of the Council on Ethics to consider the behaviour of companies, not possible violations of international law conducted by states or other parties."[227] It determined that the electricity supply interruption was temporary, and that it was not possible to tie the humanitarian situation in Gaza to the actions of the IEC.[228] In the absence of current violation, the only issue remaining was whether there was a unacceptable risk of future breaches.[229] Because there did not appear to be a current indication of future reduction, the Council decided against a recommendation of exclusion—at least for the moment.[230] The opportunity to

222. "Assuming, however, that there did exist a plan to escalate the rate of reductions in electricity supply, as suggested in the OCHA report, it seems clear that this plan has not been implemented." *Id.* at 5.

223. "The question of legality of IEC's reduction in electricity supply to Gaza has been the subject of a petition for temporary injunction brought before the Supreme Court of Israel. The petition is brought on by a group of private individuals and NGOs in Israel. In the Supreme Court ruling, dated January 27, 2008, it was found that the reduction in electricity supply is not unlawful." *Id.* at 2.

224. *Id.* Instead, finding the question technically complex, the Council "assumes that, in practice, it is probably difficult to distribute the power according to humanitarian needs." *Id.* at 3.

225. "The ambassador described the security situation for the civilian population of Israel which is subjected to repeated rocket attacks from Gaza. She also explained that employees of IEC have been targeted by gunfire when they have conducted maintenance work on the power lines which supply Gaza from Israel, and that Israeli power plants which produce electricity for Gaza are also targeted by rockets launched from Gaza." *Id.*

226. "The Palestinian energy officials confirm that there are no ongoing reductions in the electricity supply to Gaza. The 0.5% reduction by IEC, which OCHA and other sources has referred to earlier, had in fact ceased." *Id.*

227. *Id.* at 4. It also disregarded the connection between the State of Israel as majority shareholder of IEC. *Id.*

228. *Id.*

229. *Id.*

230. *Id.* at 5. The intellectual journey was a bit curious:

> The Council finds it difficult to have a clear opinion on the likelihood of such possible, future reductions in the supply of electricity to Gaza. Companies' past actions can, however, give indications to future behaviour. Considering the situation in general and

revisit the issue arose again in the aftermath of the Israeli incursion into the Gaza Strip in the waning days of the second Bush Administration.[231]

It is difficult to avoid the political in this consideration. It is also harder to conceive of a state entity in this case acting beyond the wishes of the Norwegian state with respect to its involvement in the economic aspects of this war. At the same time, issues of complicity have now become much more important for investors under instruments like the OECD's Guidelines for Multinational Corporations.[232] International consensus on corporate and financial complicity in violations of international law has forced private entities to be more aware of the political consequences of private economic activity. Those obligations, and consequences, fall equally on states seeking to intervene in private markets under similar conditions. But the result is perverse—the SWF that seeks to function like a private entity is now forced to factor political consequences into its private activities. In that case, SWF would most likely look to their owner's own political interests rather than the generalized interests in the avoidance of violations of international law.[233] Indeed, in a complaint that was decided after the IEC investigation, issues of complicity played a key role in efforts to extend political action against the State of Israel by the Norwegian government through its Fund.[234] The Recommendation of the Council of Ethics

> the repeated rocket attacks against Israel, it cannot be ruled out that future situations could arise where IEC again is instructed to reduce the electricity supply to Gaza. Assuming, however, that there did exist a plan to escalate the rate of reductions in electricity supply, as suggested in the OCHA report, it seems clear that this plan has not been implemented. It also seems clear that there have been no repetition of the power cuts.

231. *Id.* at 4-5.

232. *See* discussion *supra* notes 35-38 and accompanying text.

233. This is considered in Backer, *Rights and Accountability*, *supra* note 36.

234. Norwegian Ministry of Fin., *Recommendation on the Exclusion of the Company Elbit Systems, Ltd.* (Sept. 3, 2009), http://www.regjeringen.no/en/dep/fin/Selected-topics/the-government-pension-fund/ethical-guidelines-for-the-government-pe/Recommendations-and-Letters-from-the-Advisory-Council-on-Ethics/the-council-on-ethics-recommends-that-th.html?id=575451 (last visited Nov. 12, 2009) [hereinafter *Exclusion of Elbit Systems*]. In the related press release, the Norwegian Ministry of Finance made clear the conflation of state policy and ethics in the operation of the Fund's investment strategies:

> The Ministry of Finance has excluded the Israeli company Elbit Systems Ltd. from the Government Pension Fund—Global, on the basis of the Council on Ethics' recommendation. The Council on Ethics has found that investment in Elbit constitutes an

was based almost entirely on complicity grounds, and an unconcealed political determination, grounded in its assessment of the legal ramifications of a variety of courts, the importance of which the Ethics Council evaluated using its own criteria, that the Israeli State's construction of its "separation barrier" constituted important violations of international law.[235]

### 3. Investment Sanctions Against Burma

In its 2007 Annual Report,[236] the Ethics Council summarized its actions with respect to companies operating in Myanmar (formerly Burma). The Council noted that at the request of the Ministry of Finance,

> over a longer period of time we have monitored several companies with operations in Burma. . . . The Council's mandate indicates that the presence in, and the generation of revenue for oppressive states cannot, in itself, be sufficient for exclusion from the Fund. There must be a more direct link between the company's operations and the human rights violations in ques-

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> unacceptable risk of contribution to serious violations of fundamental ethical norms as a result of the company's integral involvement in Israel's construction of a separation barrier on occupied territory. "We do not wish to fund companies that so directly contribute to violations of international humanitarian law," says Minister of Finance Kristin Halvorsen.

Press Release, Norwegian Ministry of Fin., *Supplier of Surveillance Equipment for the Separation Barrier in the West Bank Excluded from the Government Pension Fund—Global*, (Sept. 3, 2009), http://www.regjeringen.no/en/dep/fin/press-center/Press-releases/2009/supplier-of-surveillance-equipment-for-t.html?id=575444 (last visited Nov. 12, 2009).

235. *Exclusion of Elbit Systems*, *supra* note 234. The Council concluded:

> Israel, however, has chosen to build a separation barrier of whose extension nearly 90% is located in areas occupied by Israel. This, and the humanitarian problems that the choice of the route causes, constitute the problematic aspects of the separation barrier. . . . In general, the Council on Ethics' task is to evaluate issues specifically related to companies, not possible violations committed by states or other actors. In this case, however, the Council on Ethics is faced with an assessment of a company commissioned by its own state authorities to commit acts that must be deemed illegal.

*Id.* at 8-9. In addition, there appeared to be a suggestion that the recommendation was grounded in Elbit Systems' refusal to cooperate. *See id.*

236. *See Annual Report 2007*, *supra* note 175, at 82-85 (Council on Ethics' Assessment of Companies With Operations in Burma).

> tion. Based on our knowledge of Burma from previous and on-going studies, we assume that larger infrastructure projects in Burma imply a great risk of gross and systematic human rights violations related to such work.[237]

The Ethics Council first noted that the Funds had no direct investment in Burma, but that a number of companies in which the Fund invested did have operations in Burma.[238] It noted that in its prior review of economic activity in Burma, in 2005, "the Council regarded, as general point of departure, that the risk of grave human rights violations in connection with construction of infrastructure in Burma is considerable. The situation has hardly improved since then. Grave human rights violations such as forced displacement of people and extensive use of forced labour can be expected."[239] The problem is not direct commission of human rights violations, but complicity in their commission of human rights violations by the Burmese government.[240]

The Council engaged in extensive investigations,[241] some of which also relied heavily on the Norwegian diplomatic corps in Southeast Asia.[242] It determined that efforts to construct a gas pipeline from Burma to China was suspect.

> If companies in the Fund's portfolio were to enter into contract agreements regarding the construction of such pipelines, the Council may recommend the exclusion of these companies already from the time of entering into the agreements. Because such undertakings would most likely involve an unacceptable

237. *Id.* at 5.

238. "The majority of these companies belong to the energy, mining, oil and gas, hydroelectric power, telecommunications, banking, pharmaceutical and hotel sectors. The companies are listed on, among others, the South Korean, Thai, Singaporean and French stock markets." Letter from Gro Nystuem to the Ministry of Finance (Oct. 11, 2007), *in* Council on Ethics for the Gov't Pension Fund, *Annual Report 2007*, *supra* note 173, at 82.

239. *Id.* at 83.

240. *See id.*

241. Thus, "the Council has obtained information from the concerned companies as well as from different organisations. The Council's secretariat has also temporarily employed a staff member who, in February this year, was in the border areas between Burma and Thailand to gather information on the human rights situation related to construction projects. Also, during a visit to India in February, the secretariat sought to clarify the status of the cooperation between India and Burma for the construction of a gas pipeline." *Id.*

242. "[I]n October of this year the secretariat will meet with Burmese citizens in exile, various organisations and the Norwegian embassy in Bangkok to gather additional information." *Id.*

> risk of contributing to human rights violations, it is not considered necessary to wait until the violations actually take place.[243]

On the other hand, the Ethics Commission declined to recommend exclusion of the South Korean company Daewoo for the export of military hardware and technology to Burma.[244] But the reasons were technical: the violations had occurred in the past, they were unlikely to recur because the officials involved had been indicted in South Korea for breach of national law.[245] The Council, though did note that though the sale of technology for the production of artillery shells does not fall within the weapons prohibitions of the Guidelines, their sale to a regime determined to be repressive might still constitute a particularly serious violation of fundamental ethical norms under the Guidelines.[246] Lastly, the Council warned that investigations were ongoing with respect to two other Burma related matters. The first focused on entities participating in the construction of hydroelectric power plants in Burma.[247] The second involved entities involved in mining operations in Burma.[248] "The Council's work on information gathering on these topics continues."[249] Here again, the political factors that motivated the approach to the Israeli issues underlie the relationship between the Norwegian state, the Global Fund and the objects of its investment.

### B. *Development and Use in Macroeconomic Policy: the 2008 Financial Crisis*

The criteria for investment in companies, and perhaps ultimately for grounding activity as shareholder, suggests the way in which funds, as investors, might help shape microeconomic policy.[250] But SWFs may

243. *Id.* at 84.

244. *See id.*

245. *See id.*

246. *See id.* (referencing Guidelines ¶ 2 subpar. 3).

247. "Such projects have previously been known to lead to forced displacement of people and to forced labour." *Id.* at 85.

248. "It must be assumed that conditions related to mining in Burma can be severe, both in terms of environmental aspects, working conditions and effects on livelihood for the population in proximity of the mines. Nor can it be ruled out that forced labour is used, either in the mining operations themselves or when clearing areas for new mines." *Id.*

249. *Id.*

250. *See* discussion *supra* Section II; *see also Santiago Principles, supra* note 8, at 13, GAPP 3 Principle, Explanation and Commentary ("Since SWFs are often created for macroeconomic purposes, their operations should support and be consistent with a sound overall macroeconomic policy framework").

also shape macroeconomic policy in a way that is harder to square with the private and participatory character of these funds. To suggest the parameters of this activity within the Norwegian Funds, it is only necessary to examine the conduct of these funds during the early course of the global financial downturn that became generally recognized during the summer of 2008. The fairly fast pattern of activity by the funds is nicely indicated by the changing complexion of Norwegian fund activities from mid 2008 on.[251] The changes took two forms. The first was a retreat from investments abroad to a more traditional and sovereign use of Global Fund assets to support domestic economic programs. The second was a greater focus on strategic Global Fund investment to meet the political requirements of Norway, especially with respect to investment in emerging economies. Together they suggest the limits of the formally public/functionally private model grounded on a passive private investor behavior model, especially during turbulent financial periods. Each is explored below.

### 1. From Outbound to Inbound Investment

In the Spring of 2008, confidence in the performance of markets worldwide led to a suggestion that the Global Fund change its investment strategy to increase the allocation for equity investments from 40% to 60%.[252] It was also reported that "[t]o facilitate such investment, Slyngstad asked the government to let the central bank-run fund take stakes of up to 15 percent in individual companies, up from a 5

251. For a general report on these issues, *see* GOVERNMENT PENSION FUND 2008, *supra* note 139.

252. John Archer & Wojciech Moskwa, *Norway Oil Fund Big Buyer of Stocks, Eyes New Deals*, REUTERS (Oslo), May 29, 2008, *available at*: http://www.reuters.com/article/reutersEdge/idUSL2967976620080529?pageNumber=1&virtualBrandChannel=0 (last visited Feb. 1, 2009). The article indicates that the fund is shifting to a 60 percent allocation in stocks from 40 percent, and that just over 50 percent of the equity portfolio is in Europe. The article indicates that Norway's SWF is buying equities and selling bonds to make this transition. According to the article, Mr. Slyngstad [the NBIM manager] indicated that the fund's subprime exposure "is minimal, less than .4 percent of the fund . . . We regard volatile markets as . . . an opportunity." Also, according to Mr. Slyngstad, the fund has been approached to take part in "quite a few deals" and he has formed a special division (Capital Strategy Division) to invest larger, more concentrated equity stakes in companies: "That would represent a new departure for the fund—concentrated large ownership, quite likely for a longer period—using our size and our longer investment horizon. . . . If for some reason we would participate in a recapitalization of a large bank with a large stake, basically this group would be doing it. . . . A fund of our size is quite likely to have been shown quite a few deals. . . . I wouldn't say that we have not participated, but I won't confirm that we have either." *Id.*

percent limit. The government decided on a 10 percent limit."[253] The Ministry of Finance decided to increase the allocation to equities in the Global Fund from 40% to 60%, with an actual increase, at the end of the third quarter, of the allocation to equities to 53%.[254] "The expansion continued to property and property development through the summer of 2008.[255] This had been a subject of discussion in the prior year and reporting to the Storting in 2007.[256]

At the same time, the Global Fund continued to invest heavily in the financial sector.[257] By August 2008, this had become a source of concern.[258] The bottom fell out in the late summer, with the collapse of

253. *Id.*

254. Press Release, Norges Bank, Substantial Market Fluctuations and Considerable Uncertainty (Nov. 25, 2008) *available at* http://www.norges-bank.no/templates/article____72934.aspx (last visited Dec. 16, 2009).

255. Chanyaporn Chanjaroen, *Helical Bar in Talks Over Potential Takeover, Observer Reports*, BLOOMBERG.COM, Aug. 3, 2008, http://www.bloomberg.com/apps/news?pid=newsarchive&sid=auREVWJejayg (last visited Feb. 1, 2009) (reporting that Helical Bar Plc was "in talks with Norway's sovereign wealth fund which may lead to a takeover of the U.K. property developer," according to an unidentified person close to the company). According to the report, the discussions were preliminary and could result in a large cash injection for the company. "The Norwegian fund considered appointing Helical Bar Chief Executive Officer Michael Slade to run its European property investments." However, a spokesman for Helical Bar had declined to comment. *Id.*

256. *See Report No. 16, supra* note 138, at 23-25.

257. Gore Gareth, *Norway State Fund Buys Banco Santander Stake, Economista Says*, BLOOMBERG.COM, Aug. 20, 2008, http://www.bloomberg.com/apps/news?pid=newsarchive&sid=a3e4TvTljhL8 (last visited Feb. 1, 2009) (reporting that Norway's sovereign wealth fund bought 800 million-euro ($1.8 billion) stake in Spain's lender Banco Santander SA according to the state-managed investment fund). "Norges Bank purchased a 1.12 percent stake in the lender." *Id.* Additionally, the fund bought a 5.08 percent stake in May, valued at 300 million euros in the Santander's Sovereign Bancorp Inc.'s unit. *Id.*

258. Nina Berglund, *Oil Fund Takes 'Minor' Hit from U.S. Mortgage Crisis*, AFTENPOSTEN [THE EVENING POST] (Nor.), Aug. 26, 2008, *available at* http://www.aftenposten.no/english/business/article2618343.ece (last visited Feb. 1, 2009). The article mentioned Norway's SWF exposure in the U.S. mortgage companies Fannie Mae and Freddie Mac. According to the article, Yngve Slyngstad indicated that the fund's total Fannie Mae and Freddie Mac exposure amounts were about NOK 88 billion (USD 16.36 billion):

> "[e]ighty-eight billion (crowns) is relatively little in relation to other central banks, but it is that big because we consider this the second most secure investment in the United States," Slyngstad said. The oil fund's holdings in Fannie Mae and Freddie Mac bonds have fallen from a value of NOK 129 billion at the end of 200, Slyngstad said while releasing the fund's second-quarter results. The fund, formally called The Government Pension Fund—Global, grew by 2.4 percent in the second quarter from the first, reaching NOK 1.992 trillion (USD 370.8 billion) though it had a negative return on

Lehman Bros, in which the Global Fund had invested heavily.[259] The Global Fund, also suffered losses with the collapse of Fannie Mae and Freddie Mac, though it had better anticipated this collapse.[260] These losses prompted a response from Norges Bank.[261]

The effects of the financial collapse were not just felt in the value of the Global Fund. It also had an effect on the ability of the Global Fund managers to pursue its conventional investment strategies.[262] Accord-

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> investment. The fund's return was a negative 1.9 percent in the second quarter, hit by turmoil in financial markets.

*Id.*

259. Wojciech Moskwa & Camilla Knudsen, *Norway's Wealth Fund Says Was Prepared for Lehman*, REUTERS (OSLO), Sept. 15, 2008, *available at* http://www.reuters.com/article/marketsNews/idUSLF71090920080915?sp=true (last visited Feb. 1, 2009). They reported that Norway's SWF was "prepared for the bankruptcy filing by U.S. bank Lehman Brothers, in which it held more than $840 million worth of stocks and bonds at the end of 2007." According to the article, the Government Pension Fund—Global "owned .27 percent equity stake in Lehman Brothers at the end of 2007" worth $88.78 million, and it held Lehman Brothers Holdings Inc. fixed income securities worth 4.38 billion crowns. The fund also held approximately "1.55 billion crowns of debt from other Lehman vehicles." *Id.*

260. Gregory Roth, *Norway Finds Virtue (and Value) in Transparency*, N.Y.TIMES, Sept. 26, 2008. The report indicated that over the first six months of 2008, the fund reduced its holdings of Fannie Mae and Freddie Mac debt by almost a third. "Does this reflect a loss of confidence in the debt of these two lending giants, which are now backed explicitly by the United States government?" asked Mr. Roth. "It doesn't reflect a lack of confidence in these institutions or the U.S. system. I think you rather have to say that there are other investment opportunities in the United States that may look equally attractive or more attractive for the moment," said Mr. Slyngstad. But there was no further elaboration on this issue. *Id.*

261. Mr. Yngve Slyngstad, CEO of Norges Bank Investment Management, made the following remarks when commenting on the performance of the fund in a November 25, 2008 press release published by Norges Bank:

> the third quarter of 2008 was an unusually demanding quarter for the management of the Government Pension Fund—Global. Uncertainty in financial markets increased dramatically, and this affected the return on the fund. The return on the fund in the third quarter was −7.7 percent in international currency. The return on the fund was 1.8 percentage points lower than that on the benchmark portfolio defined by the Ministry of Finance.

Press Release, Norges Bank, *supra* note 254.

262. David Ibison, *Norway to Dip Into $332bn Oil Fund*, FINANCIAL TIMES.COM, Dec. 15, 2008, *available at* http://www.ft.com/cms/s/0/c601f6aa-ca47-11dd-93e5-000077b07658.html (last visited Feb. 1, 2009). By December 14, 2008, David Ibison reported in the Financial Times.com that Norway would tap its sovereign wealth fund in January 2009 to finance a new fiscal spending package in order to offset the rapid slowdown in Norway's economic growth next year. The article mentions the following statements by Jens Stoltenberg, Norway's prime minister: "Jens Stolten-

ing to the Summary of the 2008 Q3 Report by NBIM,[263] the return for the quarter was 7.7%—the lowest in the fund's history. The Report noted:

> The turmoil in global equity and fixed income markets has resulted in major variations in the market value of the fund. The fund's expected absolute volatility is a statistical measure that gives a model-based estimate of "normal" variations in its market value over the coming year. Since summer 2007, market movements have been far from normal, making the model less accurate than before. Market fluctuations as measured by absolute volatility have increased since summer 2007.[264]

These losses had effects on Global Fund management. By December 16, 2008, it is reported that Norway is the latest country to plan a fiscal stimulus to be rolled out in early 2009 to ramp up domestic spending. According to Ziemba, "Norway's stance was already expansionary. Its fiscal rule allows it to spend up to 4% of the GPF's assets (the assumed return on investment in most years) to meet its non-oil deficit."[265] At the year's end, Norges Bank issued a press release indicating that Norges Bank will not purchase foreign exchange for the Global Fund in January 2009. According to the press release, "the Fund's foreign exchange requirements are partly met by the state's direct financial interest in petroleum activities (SDFI) and partly by Norges Bank's purchases in the market. The Ministry of Finance determines the size of the monthly allocations to the Fund."[266] In addition, the Global

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berg, Norway's left-wing prime minister, said in an interview the government will unveil spending measures in January on top of its previously announced expansionary budget for 2009." Stoltenberg stated, "we have held back and been restrictive in our use of oil revenues in strong times but we can start to spend more now that we see a downturn coming." *Id.*

263. NORGES BANK, QUARTERLY REPORT Q3 [2008], *available at* http://www.norges-bank.no/upload/72947/spu_kvartalsrapport%20q3-english-internett.pdf.

264. *Id.*

265. Rachel Ziemba, *Raiding The Sovereign Rainy Day Fund*, RGE ANALYSTS ECONOMONITOR, Dec. 16, 2008, *available at* http://www.rgemonitor.com/economonitor-monitor/254790/raiding_the_sovereign_rainy_day_fund (last visited Feb. 1, 2009). The report also noted that "Norway could have to draw on its principal not just on the income on its investments." *Id.*

266. Press Release, Norges Bank, Norges Bank's Foreign Exchange Purchases in January 2009 (Dec. 31, 2008) *available at* http://www.norges-bank.no/templates/article____73162.aspx (last visited Dec. 16, 2009). Norges Bank's purchases of foreign exchange are equal to the difference between the allocations and the SDFI's estimated foreign exchange revenues. Adjustments are made for any revisions of estimates for the previous month. As a result, the daily purchases may vary from one month to the next. The daily foreign exchange purchases are

Fund moved more aggressively to protect its assets. In December 2008, for example, NBIM "filed a law suit in Maryland, USA, seeking to prevent Constellation Energy Group [in which NBIM owns 4.8 percent] from convening a special shareholder meeting on December 23 to vote on a takeover by MidAmerican Energy Company, a unit of Berkshire Hathaway."[267] As a consequence, the Global Fund, like other SWFs began to perform more like a traditional reserve fund—sovereign and conventional—than a functionally private and separate investment vehicle. The Norwegian Fund was sovereign after all.[268]

But most importantly, the losses and effects of the crisis resulted in a diversion of the Global Fund assets for domestic purposes. The initial focus was on the use of the state Pension fund, rather than the Global Fund for that purpose.[269] By the end of January funds otherwise allocable to the Global Fund were being diverted to fund a domestic stimulus package.[270] The Global Fund appeared to be going from

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determined for a period of one month at a time and are published on the last business day of the preceding month." *Id.*

267. Press Release, Norges Bank, NBIM Seeks Court Decision to Delay Constellation Shareholder Vote on Acquisition by MidAmerican (Dec. 17, 2008) *available at* http://www.norges-bank.no/templates/article____73134.aspx (last visited Feb. 1, 2009). According to Anne Kvam, the Head of NBIM Corporate Governance, "We are one of the biggest shareholders and take these necessary steps in order to safeguard our financial interests. In our opinion, the MidAmerican agreement undervalues Constellation, and we expect the board to work for a solution that offers the highest value opportunity." *Id.*

268. *Id.* "The escalation of the financial crisis and collapse of commodity prices likely only accelerated the trend in which sovereign funds or the governments that sponsor them are increasing their spending at home. Many other funds have also announced support of their financial sector or fiscal stimulus to support growth." Rachel Ziemba, *Raiding the Sovereign Rainy Day Fund*, Roubini Global Economics, Dec. 16, 2008, *available at* http://www.roubini.com/globalmacro-monitor/254790/raiding_the_sovereign_rainy_day_fund (accessed Dec. 25, 2009).

269. *See PM: Norway to Spend More Oil Money in 2009 to Deal with Financial Crisis*, CHINA VIEW, Jan. 8, 2009, *available at* http://news.xinhuanet.com/english/2009-01/08/content_10621343.htm (last visited Feb. 1, 2009) (indicating that Norway will spend more money from the state pension fund to support the economy in the global financial crisis). Norwegian Prime Minister Jens Stoltenberg is quoted saying, "[i]n 2009 we will use much more of the oil income than justified by the expected returns from the pension fund" in a speech at the Annual Conference of the Confederation of Norwegian Enterprise. *Id.* Also, Mr. Stoltenberg indicated that the government could use up to 4 percent of the $300 billion dollar pension fund and that "the cash would be used for boosting employment and securing Norway's generous welfare state." *Id.* This decision will be presented on January 26, 2009. In the meantime, the government has pledged a fiscal stimulus package this month to keep Norway's sharply slowing economy from recession. *Id.*

270. Norway "unveiled a NKr20bn ($3bn, €2.25bn) fiscal stimulus package as it starts to use its massive oil wealth to boost growth and employment in its struggling economy. The Nordic country of just 4.7m people has amassed $370bn in oil revenues—the world's second largest sovereign wealth fund, after Abu Dhabi's—and is now starting to use it to soften the effects of an

external investor to another source of revenue for internal sovereign purposes.

2. From Private Investor to Strategic Investment

Thus, by the end of January 2009, the focus of the Norwegian SWF appeared to change. It had moved from the formally public/functionally private model grounded in a non-interventionist private actor investment framework to another source of state funds for domestic needs. An article published by Bloomberg on January 22, 2009, suggested that "financial institutions will be unable to tap more capital from sovereign wealth funds in China, the Middle East, Norway and Russia as those funds focus on shoring up domestic markets."[271] But it had changed in more telling ways as well. Even as it began deploying its funds to shore up its internal economy, the Fund continued to try to use its funds for global macroeconomic purposes. That was in line with an assessment of the investment strategy of the Global Fund with respect to emerging economies.[272] Indeed, the idea in these cases was that intervention and engagement were more suitable for these markets.[273]

Perhaps the most telling intervention occurred in late 2008 in India. "In a move that will bring considerable relief to Indian equity markets roiled by the global credit crisis, the Norwegian Sovereign wealth fund (SWF), plans to invest around $2 billion (about Rs9,772 crore) in India, primarily in equities, over the next two months."[274] It is managing to do this not by fiat but by the manipulation of its objective investment standards, "because it has increased India's weightage in its investment

expected recession." David Ibsen, *Norway Dips into Oil Fund for NKr20Bn Stimulus*, FIN. TIMES, Jan. 26, 2009, *available at* http://www.ft.com/cms/s/0/5cd3812a-ebbd-11dd-8838-0000779fd2ac.html?nclick_check=1 (last visited Apr. 15, 2009) ("The new spending package comes on top of a previously announced expansionary budget that was equivalent to 0.7 percent of gross domestic product and takes total government spending on the crisis to 2.3 percent of GDP—one of the most aggressive spending plans in Europe.").

271. Hu, Bei, *Financial Firms Need $1 Trillion More in Equity, Rajpal Says*, BLOMBERG.COM, Jan. 22, 2009, http://www.bloomberg.com/apps/news?pid=newsarchive&sid=az.YFoCf9J_E (last visited Dec. 20, 2009).

272. *See Report No. 16, supra* note 138, at 98-112.

273. *Id.* at 110. ("It is further suggested that corporate governance criteria should not be decisive for purposes of the inclusion or exclusions of markets in or from the investment universe or the benchmark portfolio. The Bank is of the view that the best corporate governance effects are achieved through presence and active involvement, and that such effects will in large part concern company specific matters.").

274. Shankaran, *Norway Fund, supra* note 68.

portfolio."[275]

The Norwegian government indicated that investments would take place between October 2008 and January 2009, pending a double taxation avoidance treaty which could have been completed as early as January 2009. Thorvald Moe, deputy secretary general in Norway's ministry of finance, indicated that the Government Pension Fund's managers recently increased India's weight from .2% to .94% because they see "potential in India, though its financial markets still have a long way to go." The investment is to take place in companies that meet the ethical standards established by the Norwegian Parliament. The article further indicates that Mr. Moe was enthusiastic about the major expansion of the sovereign fund in India, adding that this was "more than just a strategic investment." Finally, according to the article, Mr. Moe also said Norway plans to invest more in projects that propel the Clean Development Mechanism forward, as part of the Norwegian initiative on sustainable development, with special emphasis on solar energy.[276]

There are at least two principle ways of characterizing this move. On the one hand, the Norwegian SWF might be in the same position as a private investor who seeks to maximize wealth through a macroeconomic based long-term investment strategy, as Warren Buffet recently attempted.[277] It is, in this case, acting as a private investor in markets outside of its territory and outside of its power to regulate. It is because the action is undertaken both in the ordinary course of such investment (undertaken in the same manner of that available to private investors) and not subject to regulatory leverage (if the investment were undertaken domestically) that one could characterize this as akin to private investment activity. And there have been great efforts to arrive at a consensus to this effect.[278] But that is not the way the Indian media see it. "An SWF is a global investment fund owned by a government. Unlike a private international investment fund, which is governed by profit motives, SWFs might have national strategic objectives that have made them controversial investment vehicles."[279]

275. *Id.*

276. *Norway Fund to Invest $2b in Indian Stocks*, BUS. STANDARD (India), Oct. 22, 2008, *available at* http://www.business-standard.com/india/storypage.php?autono=338043 (last visited Dec. 20, 2009).

277. *See infra* notes 329-30 and accompanying text.

278. *See* Law at the End of the Day, http://lcbackerblog.blogspot.com (Aug. 22, 2008 10:43 EST).

279. Shankaran, *Norway Fund*, *supra* note 68.

And one can see why: Norwegian investment will "come into the country at a time when foreign institutional investors (FIIs), the main driver of Indian stock markets, have taken out close to $11.2 billion from the country since January."[280] If the Norwegian SWF is acting counter-intuitively, then its motives must be something other than profit. Or better put, the Norwegian SWF may be wiling to accept financial losses for a greater political value vis-à-vis India. But that is not investing, that is state political activity. And in this case, this suggests that a significant (though in this case positive and welcome) intervention by one state in the internal affairs of another through the form of private participatory activity can be subsumed within the private investor model for SWFs.

It is for that reason that governments, including that of India, have viewed SWF investment as a political threat—discounting the private character of the investment as well as the power of the state to effectively regulate that private investment by foreign public organizations. That had been the position in India as late as 2007, in a speech by Reserve Bank of India Governor Y.V. Reddy.[281] But that reaction has been sidelined by the hard realities of the need for cash. The poor cannot afford the scruples of the well-off, even in matters of law. In India's case, "the government decided to follow the finance ministry's suggestion that India could at this time ill afford to be picky about the kind of overseas investors who bring in money."[282]

## V. Regulatory Implications

### A. *The Role of Investment and the Utility of the Idealized Private Investor Model*

An important element of the debate about regulatory approaches to sovereign wealth funds relates to the character of the funds' owners. The fear expressed by some is that funds serve as a covert mechanism for extending state power.[283] More importantly, there is a suggestion

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280. *Id.*

281. "India has a stake in the on-going debate by virtue of its increasing importance in global capital flows. The critical issue relates to standards of governance and transparency that are adopted by such funds and the extent of comfort that investee countries have in this regard," Reddy said." Sanjiv Shankaran, *Centre Puts SWFs Under the Scanner*, LIVEMINT.COM (India), Mar. 10, 2008, http://www.livemint.com/2008/03/10004539/Centre-puts-SWFs-under-the-sca.html (last visited Dec. 20, 2009).

282. Shankaran, *Norway Fund*, *supra* note 68.

283. Rose, *supra* note 25, at 112.

that the integrity of private markets themselves are threatened when they cease functioning as economic forums and begin to serve as another vehicle for the advancement of state political and regulatory activity. What are the roles of investment? Does the Norway SWF act as a private/public investor under the idealized private investor model? How is the wealth maximization described for the Norway SWF? Is it different than private investments? If it is different, should it matter?

For the Norwegian Fund, the answer appears simple enough—the funds ought to be treated as purely private and participatory vehicles of state investment.[284] That position is worth considering in more detail. It starts with the principle of free movement of capital and open capital markets,[285] and suggests that the participation of sovereign wealth funds might contribute to the functioning of those markets.[286] "They may therefore act as a stabilizing factor in financial markets by dampening asset price volatility and lowering liquidity risk premia."[287] Norway concedes only a limited set of restrictions "concerning national security."[288] It suggests itself and its operations as the model for sovereign wealth funds in a restrictionless environment.[289] It points to several operational factors that reinforce the idea that the funds are essentially private and participatory, rather than regulatory:

> Key factors in the management of the Fund include a high degree of transparency in all aspects of its purpose and operation, the Fund's role as a financial investor with non-strategic holdings, an explicit aim to maximise financial returns, and clear lines of responsibility between political authorities and the operational management. The management aims for international best practice, and the exercise of ownership rights is based on internationally accepted principles such as the UN

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284. *Norway's Position on Sovereign Wealth Funds*, *supra* note 118.

285. "The declaration from the G8-summit on 7 June 2007 expressed what would seem to be a sound principle: '. . . we remain committed to minimize any national restrictions on foreign investment. Such restrictions should apply to very limited cases which primarily concern national security.'" *Id.*

286. "A debate on SWF should also reflect these funds' potential to positively influence international financial markets through enhancing market liquidity and financial resource allocation. Typical characteristics of SWF are long investment horizons, no leverage and no claims for the imminent withdrawal of funds." *Id.*

287. *Id.*

288. *Id.*

289. "In relation to the current debate on SWF, the management of the Government Pension Fund—Global is often cited as an example to be followed." *Id.*

> Global Compact and the OECD Guidelines of Corporate Governance and for Multinational Enterprises.[290]

And it suggests that transparency not only serves to assuage fears but also positively contributes to market stability.[291] Having created a model of a private participatory institution, the Norwegians assert that there is no reason to treat these funds differently from other private funds.[292] Indeed, Norway's position appears to be that a SWF is sufficiently functionally private if it maintains a separation of ownership from control of the fund. As long as the political branches are not directly in control, the SWF is sufficiently insulated to be treated like a private fund.[293] In a sense they are right—to the extent that private funds also seek to regulate behavior through investment activity. Yet that sort of targeted regulatory investment contradicts the essence of SWFs as non-political and thus safe. SWFs are quite political in their objectives—but that does not make them different from other private funds.[294] It makes them different from the ideal private investor behavior model that has been put forward to make them seem non-threatening. Yet they are threatening, but only in the same way that large private funds are threatening to national economies.

In this respect they mirror the conclusions of influential academics as well as the framework within which important voluntary codes have been drawn. Lurking beneath these notions is the idea that, to the extent that sovereign funds mimic private funds in objectives and operations, and to the extent that a wall can be erected between the political/regulatory function of the state and its private/regulatory activities, then at least with respect to those private activities, the state owned funds ought to have the same rights (and be burdened with the same obligations) as private funds. For that purpose, of course, both

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290. *Id.*

291. "Furthermore, openness about the fund management can contribute to stable international financial markets, as well as exert a disciplinary pressure on the management that improves its quality." *Id.*

292. "However, we see no cause for regulations that would restrict the present investment activities of our Fund, or any regulation imposing restrictions on SWF over and above those applying to non-SWF investors." *Id.*

293. *See Report No. 16*, *supra* note 138, at 36 ("The international debate on Sovereign Wealth Funds places a strong emphasis on a clear separation of roles between the owner (represented by the political authorities) and the asset manager, and openness to operational management.").

294. *See id.* at 60 (comparing Global Fund with other investment funds). Though the primary focus there is on performance, there is also a focus on investment strategy on this sort of comparative basis. *See id.* at 77, 100, 109 (focusing on the behavior of other large funds).

the sovereign wealth funds and their supporters within academic and business circles have embraced the following, usually unstated, assumption that there are sets of presumptions and behaviors that can serve to define the ideal private investor (among which equal treatment is logical and fair), and to distinguish from the behavioral characteristics of other types of investors (states and other public entities). It presumes that a state can shed its sovereign character under certain circumstances and behave like other juridical persons (corporations and the like).

Those were the ideas underlying the basic framework of the Santiago Principles. The resulting "deal" presupposes the possibility of distinguishing public from private investment objectives, and political from financial motivations.[295] European Union law has moved much further in defining the contours of this notion than most other jurisdictions. This has occurred in the context of efforts to harmonize traditional state authority to invest in national industry with the strengthened obligations under the European Community Treaty to foster free movement of capital and restrain states in subsidizing their own businesses for competitive advantage within the European market. European law has tended to closely regulate state activity that is deemed sovereign and permit only a very narrowly drawn area of activity where states can demonstrate actions that mimic those of a "private investor." Thus, for example, the European Court of Justice stated "that the purchase by a Member State of equity interests in a company might be characterized as a 'state aid' under the competition provisions of the EC Treaty . . . and its compatibility with the common market must be assessed on the basis solely of the criteria laid down in that provision" under the competition provisions of the EC Treaty.[296]

The European Court of Justice has applied a private investor test in that context, explaining that "it is appropriate, in the present case, to apply the test of a private creditor in a market economy."[297] The framework is meant to be grounded in parity between state and private

295. *See* discussion *supra* Section II.

296. Backer, *Private Law of Public Law*, *supra* note 1, at 1831-32 (referencing Art. 87(1) of the E.C. Treaty and Case 323/82, Intermills SA v. Comm'n 1984 E.C.R. 3809).

297. The ECJ explained that in that case the public actor failed to "act as a public investor acting in a manner comparable to that of a private investor pursuing a structural policy—whether general or sectoral—and guided by the longer-term prospects of profitability of the capital invested. That public body had in fact to be compared to a private creditor seeking to obtain payment of sums owed to it by a debtor in financial difficulties." Case T-198/01, Technische Glaswerke Ilmenau GmbH v. Comm'n, 2004 E.C.R. II-2717 ¶ 99, *available at* http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:62001A0198:EN:HTML.

investors. The distinction is between action that can be characterized as private and that which is sovereign and regulatory, albeit indirectly. "[W]hen injections of capital by a public investor disregard any prospect of profitability, even in the long term, such provision of capital must be regarded as aid within the meaning of Article [87] of the Treaty."[298] Treaty restrictions on the regulatory activities of Member States, then, might not apply where the actions are what one might expect from a purely private actor in private markets. For that purpose, it requires a determination "whether, in similar circumstances, a private industrial group might also have made up the operating losses of the four subsidiaries between 1983 and 1987."[299]

Yet the Norwegians, in their reports, also suggest that this picture is not entirely accurate.[300] The Fund is operated as a private concern, but the Fund's owner has been quite vocal about the use of its funds, and the construction of an investment strategy, as part of the political agenda of the Norwegian state as it seeks to leverage its voice in global affairs—from the conduct of the Burmese state apparatus, to the resolution of the Israel-Palestine wars, to the construction of global corporate governance cultures.[301] Indeed, the Fund itself is understood as a vehicle for regulation without law, for governance beyond a state.[302] The wealth maximization or sound investment principles,

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298. Case C-303/88, Italy v. Comm'n, 1991 E.C.R. I-1433 ¶ 22, *available at* http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:61988J0303:EN:HTML.

299. *Id.* ¶ 20, (determination to be made by the EU Commission).

300. *See, e.g.*, Press Release, Norway Ministry of Finance, Government Pension Fund: Climate on the Agenda, (Apr. 3, 2009), *available at* http://www.regjeringen.no/en/dep/fin/press-center/Press-releases/2009/government-pension-fund-climate-on-the-a.html?id=554070 (last visited Nov. 12, 2009) ("The Government is also going to ask Norges Bank to prepare more documents outlining its expectations in the engagement effort with companies. One important area will be the environment, and an expectations document regarding companies' strategy on climate change is considered particularly relevant. Norges Bank has given priority to climate-change issues in its ownership work and in 2008 has taken part in several major investor initiatives.").

301. *See* discussion *supra* Section IV.

302. This position has also generated criticism, precisely because of the private character of what appears in effect to be public regulation.

> The appearance of regulation may, in some circumstances, be worse than no regulation at all. The turn to ethics as a means of improving behaviour of multinational corporations offers an opportunity but also an opportunity cost: ethics can be a means of generating legal norms, through changing the reference points of the market and providing a language for the articulation of rights; yet they can also be a substitute for generating those norms. The Norwegian Council on Ethics demonstrates both tendencies.

then, serve merely as the framework boundaries within which political activity can occur.[303] As long as, within appropriate time horizons, the Funds invest soundly, a host of other factors may come into play to determine the specific manner of investment. Therefore, the opportunity to use the Funds to project power, especially regulatory power, directly into markets, is great. That projection of power was boldly asserted by the Funds' Director General in testimony before the U.S. Congress in 2008.[304] But it is also finessed within the language of traditional financial management: "The ethical guidelines for the management of the Fund are premised on high returns over time being dependent on sustainable development, in the financial, ecological and social sense."[305] Thus reframed, there is no space for the political in the actions of the Global Fund. Indeed, all actions can be understood in their financial and economic sense, since all actions have economic effect.

But Sovereign investors are not the only investment entities with these goals and programs. Consider something as innocuous as the TIAA-CREF Social Choice Equity Fund,[306] created in 2006 within a few

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Chesterman, *supra* note 186. Professor Chesterman proposes instead that the Council either act in secret or that Norway explicitly act in its sovereign capacity through the enactment of positive law. *See id.*

303. The Norwegians put it differently, emphasizing the framework and deemphasizing the political effect.

> Two policy instruments—the exercise of ownership rights and exclusion of companies—are prescribed as tools to promote the ethical commitments of the Fund. It is emphasized that ownership interests in the companies in which the Fund invests are exercised with a view to safeguard the long-term financial interests of the Fund. The guidelines are based on the view that there is a link between sustainable economic development and sustainable social and environmental development, so that the Fund in the long run as a very diversified investor with a long time horizon will benefit from companies respecting fundamental ethical norms.

*Skancke Statement, supra* note 126, at 4.

304. *Id.* ("Norges Bank notes progress on some corporate governance issues it has raised with US authorities, but simultaneously expresses concern about lack of progress in other areas. I trust that you will interpret this as a gentle encouragement of further strengthening the already high standing of US financial markets.").

305. *Report No. 20, supra* note 144, at 16.

306. Teachers Insurance and Annuity Association–College Retirement Equities Fund (TIAA-CREF) Social Choice Equity Fund (Dec. 31, 2008), *available at* http://www.tiaa-cref.org/pdf/fact_sheets/mfs_social_choice_equity_inst.pdf (last visited March 27, 2009) [hereinafter TIAA-CREF].

years of the imposition of the Ethics Guidelines framework for the Norwegian Funds.[307] The TIAA-CREF Social Choice Fund "seeks a favorable long-term rate of return that tracks the investment performance of the U.S. stock market while giving special consideration to certain social criteria."[308] The Fund invests in a pool of roughly 3,000 U.S. companies that pass a set of screens for corporate governance and social responsibility factors.[309] The factors include many that mirror those of the Norwegian Fund's Ethics Guidelines: "strong stewards of the environment; devoted to serving local communities and society in general; committed to high labor standards; dedicated to producing high-quality, safe products; and managed in an ethical manner."[310] And like the Norwegian Guidelines, the Social Choice Fund also excludes certain industrial sectors.[311] Yet few of the companies excluded from investment under the Norwegian Ethics Guidelines are also excluded under the TIAA-CREF Social Choice Fund guidelines.[312] Moreover, the TIAA-CREF Social Choice fund acknowledges that some exclusions have a negative effect on performance.[313] But there are differences as well. The TIAA-CREF fund criteria are not applied using a transparent set of procedures. There are no mandatory rules for exclusion. And discretion is vested entirely in the managers. On the other hand, the owners of the Fund can withdraw their funds at

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307. *Id.*

308. *Id.*

309. *Id.*

310. *Compare id with* the more general framework of the Norwegian Ethics Council, *supra* notes 154-181 and accompanying text.

311. "A company's involvement in the alcohol, tobacco, gambling, firearms, military and nuclear power industries is also reviewed and integrated into the process. Because of the negative social and environmental consequences of these products and services, companies with substantial involvement are unlikely to be included in the fund." TAIAA-CREF, *supra* note 306. Of course, the sectors chosen for exclusion are different than those under the Norwegian Ethics Code. *See* discussion, *supra* Section IV.

312. Thus, for example, TIAA-CREF excludes Citigroup, Inc., General Electric Co., Schlumber, Ltd., JPMorgan Chase & Co., Merril Lynch & Co., Inc., Dow Chemical Co., Exxon Mobil Corp., AT&T, Chevron Corp., Pfizer, Inc., Wal-Mart Stores, Inc. and Anheuser-Busch. TIAA-CREF, *supra* note 306. The Norwegian Fund excludes, among others, Barrick Gold Corporation (Canada), Vedanta Resources Plc, Sterlite Industries, DRD Gold, Ltd. (Canada), Wal-Mart Stores Inc. (US), Wal-Mart de Mexico, Madras Aluminum Company (India), Dongfeng Motor Group Co. Ltd. (China), GenCorp Inc. (US), Textron, Inc., (US), BAE Systems Plc, Boeing Co., Finmeccanica Sp.A., Honeywell International Inc., Northrop Grumman Corp., Safran SA and United Technologies Corp. *Id.*

313. *Id.* (identifying for the period ended December 31, 2008, Exxon Mobil Corp., AT&T, Chevron Corp., Pfizer, Inc., Wal-Mart Stores, Inc. and Anheuser-Busch.)

virtually any time.

The similarities and differences between the Norwegian Fund and a private fund constructed along similar lines suggests the value of grounding regulatory analysis on the private character of the investment activity. If public and private funds act the same way, and privilege the same behaviors, then it makes sense to treat them the same. The real role for regulation in this context ought to be to ensure that private funds are acting like private actors, and to devise systems to police that behavior. That, in essence, is the basis of voluntary efforts like the Santiago Principles.[314] Yet it also suggests the difficulties of the simple arguments made with respect to the regulatory framework for sovereign wealth funds. It is to those difficulties that the article turns next.

### B. *The Importance of Approaches in Conceptualization of Regulatory Options*

For all the similarities, for all of the conceptual congruence, it is clear that the two funds are very different, and yet they appear to function to the same ends. It is also clear that though the objectives of the two funds may be quite similar, they are deployed differently. Moreover, fundamentally similar investment objectives clearly emerge—the private fund and the Norwegian fund both mean to make money for their owners and they both seek to further agendas grounded in substantive values that are deemed to be attainable through a program of strategic investment. It is true enough that the Norwegian investment program is substantially more elaborate, institutionalized and supported by a bureaucracy, but the functions are similar enough.

On the basis of these similarities, of course, the Norwegians and influential academics and government regulators have all argued that their treatment should be substantially the same. Because they behave alike and because they are both close to the notion of the ideal private actor, the public character of one of them ought not to make a difference. As long as the actors continue to behave like private actors, that ought to be enough of a basis on which to ground a regulatory regime. But the idealized private investor standard at the heart of the usual approach to sovereign wealth fund regulation masks more ambiguity than it resolves. There is still something that nags, or ought to, something that pulls at the corners of analysis. While public and private

314. *See generally Santiago Principles*, *supra* note 8. For a discussion, see Backer, *Regulatory Responses*, *supra* note 11.

funds act alike, they are not the same.

That "something" might be understood in one of two ways. First: The current formulation masks regulatory implications of distinctions between functionalist and formalist analysis.

Formalist analysis has as its critical marker the manner of intervention. There is a distinction between formal lawmaking and the regulatory effects of participatory actions. Form may be dispositive. If the state owns a fund, the state is the fund and the fund is a sovereign apparatus.

In contrast, a functionalist analysis looks to effects and rejects the idea of a difference between law and regulatory effects. Form is not dispositive. But what ought to be the governing law when one state seeks to invest in the economy of another state? This question has become particularly acute since the rise, over the last decade, of a number of large funds controlled by states, the purpose of which is to invest in economic entities wherever they may be domesticated. On the surface, this might suggest the best case for the equal treatment of states with private entities. In this case, unlike that in which the state always has the potential to legislate changes to its corporate law, the state stands in the same shoes as a private investor. On the other hand, the state, even as a private investor, has the power to reach deeply into the economic affairs of other states by implementing its legislative program through shareholder activism.

A functional analysis underlies most current reform efforts. The "ideal investor model" of the Santiago Principles and European Union approaches to capital movements based on a "substantially equivalent effects" standard look to effects rather than the form in which it is engaged. Both have a very specific objective—to provide a principled means of restricting host state regulatory intervention by favoring free movement of capital, whatever its source, as long as it "behaves" appropriately in the host state. Formal distinctions are of little significance. Functional equivalence—public investors appearing to all effects to behave like private investors—is all that is necessary. For that purpose, a principles-based approach is preferred. Those principles lay out the norms for behavior that is encouraged—private behavior equivalents. Disclosure serves as the principle vehicle for ensuring compliance, or informing other market actors of deviation from the norms established through these principles, an approach also applied to private pools of capital (including to some extent hedge funds in the

United States).[315] Host states are then permitted to restrict only non-conforming actors, actors who are required to "confess" through disclosure.[316]

But equally important, in this case formalist distinctions matter. And they matter because formal differences signal substantive differences that a functional analysis would hide. The critical difference is grounded in notions of coercion and in whether or not the ultimate investors have a choice in the manner in which they are represented and their funds invested. In both the public and private fund, individuals are the ultimate stakeholders and investors. It is for their benefit that these funds are created and it is their interests that they ultimately serve. Let us consider from the perspective of differences between the Norwegian Fund and the TIAA-CREF fund. The Norwegian Fund's institutional holder is the state apparatus of Norway, but the ultimate beneficiaries are the citizens of Norway on whose behalf the government acts. The TIAA-CREF funds are administered directly for the investors on whose behalf the fund managers operate. But TIAFF-CREF investors are free to exit the Social Choice Fund at will (or at least in accordance with the procedures therefore agreed to when they first invested their funds).[317] Norwegian citizens have no such right. They are bound by the choices made for them by the state apparatus. They are at least one critical step removed from the Fund. As a consequence, the TIAA-CREF fund has to be more careful and conscious of the wishes of its ultimate investors than does the Norwegian Fund. The Norwegian state is accountable to the people, but the Fund is accountable only to the state.[318] The difference is important because at this point we come back to where we started—the critical differences between a state as an autonomous

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315. *See* Press Release, U.S. Dept. of the Treasury, President's Working Group Releases Common Approach to Private Pools of Capital Guidance on Hedge Fund Issues Focuses on Systemic Risk, Investor Protection (Feb. 22, 2007), *available at* http://www.ustreas.gov/press/releases/hp272.htm (last visited Apr. 15, 2009). These bear some similarity to the Santiago Principles generally accepted principles and practices. *See generally*, *Santiago Principles*, *supra* note 8.

316. This is the core logic of the Santiago Principles, for example. "To have in place a transparent and sound governance structure that provides for adequate operational controls, risk management, and accountability." *Id.*

317. Prospectus, TIAA-CREF Funds: Institutional Class, 27, (Feb. 1, 2009), *available at* http://www.tiaa-cref.org/prospectuses/index.html (last visited Apr. 4, 2009).

318. The Norwegians, however, assert that democratic principles provide an adequate safeguard. "Institutional funds in general, and funds owned by governments in particular, face specific challenges. While individual shareholders may sell their holdings of individual assets or funds they do not find ethically acceptable, the citizens of Norway have to accept to be the ultimate owners of the companies that the Fund invests in." *Skancke Statement*, *supra* note 126, at 4.

institutional actor, and non-state actors.

Perhaps the Europeans are right—the state can never shed its character as state, as sovereign, and this character infects everything it does. If that is the case, then the arguments for asymmetric control of sovereign funds becomes stronger. On the other hand, consider the nature of the difference between the TIAA-CREF and Norwegian Fund relationship to their ultimate owners. That difference might be understood better as one similar to that between shareholders of an operating company and those of a conglomerate or holding company. If the fund is the operating company, then the direct relationship between investor and fund marks a difference between the two types of funds, again leaving the state exposed as a critical and unique actor. But this is not satisfactory either—private investment also contemplates a conglomerate model, sometimes with disastrous results.[319]

The position of states with respect to SWFs, already complicated, appears to be getting even more interesting from a legal perspective. This goes beyond the usual argument that SWF activity is political (and indirectly regulatory) rather than participatory (and essentially private) because investment decisions are made to maximize the political agendas of investing states rather than to maximize profit as more conventionally defined. That distinction is itself highly dubious. Investors sometimes invest for strategic reasons with incidental profit effects—corporate social responsibility movements attest to the popularity and legitimacy of such private investment strategies. Certainly in the United States socially responsible investing similar to that followed by the Norwegian SWF are quite respectable as legitimate private investment aims. States sometimes invest strictly to make a quick return on their investment in the narrowest traditional sense. Private investors sometimes choose to invest to use their shareholder power to effect changes in corporate culture in accordance with their values. States sometimes do the same. States sometimes work through interests in private investment funds. Private investment funds sometimes work in parallel

319. For example, fund of funds are investment funds that hold portfolios of other investment funds instead of investing directly in equity and debt securities. One commentator noted: "Regulatory oversight is necessary to limit the practices of hedge funds that exacerbate the instability of the financial marketplace and undermine soundness of the market. Moreover, in the last few years, the hedge fund industry has undergone substantial 'retailization,' expanding its customer base beyond wealthy individuals and institutional investors, particularly through 'funds of funds' that rose to public prominence with the Bernard Madoff scandal." Barbara Crutchfield et al., *The Opaque and Under-Regulated Hedge Fund Industry: Victim or Culprit in the Subprime Mortgage Crisis?*, 5 N.Y.U. J. L. & Bus. 359, 408 (2009).

with SWFs. This was the conundrum facing the Indian government:

> At one level, it is easy to identify some SWFs, such as Norway's Government Pension Fund. However, as the aim is to separate a standard foreign institutional investor driven by profit objectives from a sovereign investor with strategic objectives, complications come up. Some investors from West Asia, for instance, invest in their own capacity. However, loose governance standards can mean an individual's money snakes in and out of the country's SWF, making demarcation tough, the official said.[320]

But the equation has changed a bit. No longer worried about either private self regulation models based on transparency, and adherence to some sort of idealized "reasonable private investor" model, states are becoming more eager for the money held by SWFs and will overlook more to attract investment.[321] The U.S. has led the way on this as well.[322] The recent reluctance about SWF investment will likely give way to agreement to treat SWFs like other private investors, at least until the present crisis ends. Then we will see the expected great wave of calls for reform, regulation, and distinct treatment for state investors. It is not clear, either now or later, that such distinction is necessary as a general rule.

This brings the conceptual discussion back to where it started: sovereign funds are different because states own them. Often states also control their investment strategies and choices directly or indirectly. While this would be a matter of minor distinction were states no different from other bodies corporate, the difference in the nature of the power and function of states compared to private actors, makes the

320. Shankaran, *supra* note 281. ("Similarly, if a state-owned firm motivated by strategic aims uses a private multinational investor to invest money in specific Indian companies, identification becomes difficult, he added.").

321. But sometimes is has taken unusual form, especially as national desperation increases. *See, e.g.*, Kavaljit Singh, *Nicolas Sarkozy and Sovereign Wealth Funds*, SPECTREZINE, Nov. 3, 2008, http://www.spectrezine.org/europe/Singh.htm (last visited Apr. 3, 2009) ("In a hard-hitting speech to the European Parliament in Strasbourg (France) on October 21, French President Nicolas Sarkozy proposed that European countries should create their own sovereign wealth funds to protect national companies from foreign predators."). The French leader argued, "I'm asking that we think about the possibility of creating, each one of us, sovereign funds and maybe these national sovereign funds could now and again coordinate to give an industrial response to the crisis," he told members of the European Parliament. *Id.*

322. *See* Law at the End of the Day, http://lcbackerblog.blogspot.com (June 6, 2008 15:42 EST).

problem of sovereign wealth funds distinctly political. But states tend to assert diminishing sovereign power the farther beyond their territory that they seek to assert their political power. And it is possible for a state to limit its behavior to mimic that of private actors. States have appeared to signal a willingness to attempt this in the operation of sovereign wealth funds. Just as corporations now are vested with both the obligations and rights of sovereigns under certain circumstances, at least in certain soft law regimes,[323] so states might be granted the obligations and rights of private actors when they seek to act in ways that mimic those of private actors outside their national territory. However, they will never be private actors. And though they mimic an ideal private investor, they will invariably act in ways that necessarily are geared to the furtherance of state policy and the extension of state power beyond the state. The Norwegian Fund strongly evidences both tendencies—private conduct for regulatory purposes under a framework that is about private (wealth maximization). Ambiguity, in this case, brought by the conflation of public and private regulatory models, cannot breed regulatory certainty. But that uncertainty also breeds regulatory opportunity.

### C. *Participation Versus Regulation as an Alternative to the Public/Private Model*

There is a tempting but false parallel that might be drawn between the discussion of the regulatory framework of sovereign wealth funds and the interventionist activities of governments in response to the financial crisis that started at the end of the first decade of the 21st century. That parallel is worth considering to emphasize the distinctive issues at the heart of sovereign wealth fund regulation. The distinction is grounded in the difference between regulatory and participatory activities within markets.

The brunt of state based regulatory reaction to the financial crisis has been traditional and conventional. States have sought to intervene directly in their markets and aid domestic enterprises. The American Emergency Economic Stabilization Act of 2008 is typical of these efforts.[324] Most of the schemes floated by desperate states are both

323. *See* Backer, *supra* note 36.

324. For an analysis see Law at the End of the Day, http://lcbackerblog.blogspot.com (Oct. 15, 2008, 01:13 EST).

highly regulatory and interventionist.[325] Such attempts tend to revolve around a willingness to provide ailing sectors of the economy with direct or indirect infusions of capital in return for acceptance of both macro and micro regulation.[326] Micro regulation is taking the form of the petty and vindictive, though as a post facto effort it serves merely as a gesture to assuage the public and preserve the images of politicians as somehow working in the public interest. Macro regulation is taking the form of changes in the regulation of banks and their financial arrangements.[327]

Yet there is an element of hybrid action as well. Governments will be taking interests in many of the entities they are "saving" in the form of warrants from banks and other forms of equity stakes in other enterprises taking state largess.[328] These arrangements will pose something of a conceptual difficulty for action in the future. The character of those investments—and the power of the state as "shareholder" rather than regulator—remains nebulous at best. On the one hand, the state is, as a formal matter, investing in the market in the same way as any other private investor. To the extent it is participating in the market rather than regulating it, the investment might be characterized as private rather than public. On the other hand, this private investment is undertaken in entities over which the "investor" has strong regulatory

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325. Welcoming the summit details, Sarkozy said the meeting would be "followed by several others aimed at rebuilding the international financial system and making sure the current crisis does not happen again thanks to better regulation and more efficient surveillance of all players." Jeremy Pelofsky, *Financial Crisis Summit Set for November 15*, REUTERS, Oct. 22, 2008.

326. That, of course, was the essence of both stimulus packages enacted at the end of the second Bush administration and the beginning of the Obama administration. *See* Matthew Hadro, *Government Can Influence Banks with $250 Billion Stock Buy, Say Economists*, CNSNEWS.COM, Oct. 30, 2008, http://www.cnsnews.com/Public/content/article.aspx?RsrcID=38411 (last visited Mar. 30, 2009) ("The Emergency Economic Stabilization Act of 2008, passed by Congress and signed into law by President Bush on Oct. 15, includes a $250 billion government purchase in 'senior-preferred shares' in U.S. banks. The purchase is designed to infuse capital into the banks so they can keep credit flowing and apparently help stabilize the market."). The relationship of AIG to the government is a widely publicized case in point. *See* Matthew Karnitschnig, et al., *U.S. to Take Over AIG in $85 Billion Bailout; Central Banks Inject Cash as Credit Dries Up*, WALL ST. J., Sept. 16, 2008, at A1 ("It puts the government in control of a private insurer—a historic development, particularly considering that AIG isn't directly regulated by the federal government.").

327. *See* Hadro, *supra* note 326.

328. This is not merely a U.S. phenomenon. *See, e.g.*, V. Phani Kumar, *Japan Considering Direct Share Purchase: Report*, MARKET WATCH, Feb. 24, 2009, *available at* http://www.marketwatch.com/story/japan-government-considering-direct-share-purchases ("The government is considering direct market purchases amid concerns that falling share prices would boost losses among securities held by domestic financial institutions and companies, aggravating conditions in a deteriorating economy, the report added.").

authority. Indeed, the "investor" has utilized this regulatory power as a critical component of its private investment decision. On a substantive basis, then, the private investment appears to be incidental to the regulatory activity of the state.

There have also been highly publicized private efforts to shore up confidence (and free up capital) for the debt markets. Among the more well known of these private efforts was that of Warren Buffet to inject billions into the financial markets. The efforts by the larger and more stable investment houses to shore up their weaker members were another example. To date, though, these grand gestures have had little short-term effect.[329] But the effort might be viewed as a private effort not so much to shore up the private markets but to prod appropriate state intervention.[330]

Lastly, there have been efforts, like those that led to the creation of the Santiago Principles, to develop consensus based soft law at the supra-national level for transposition within the national legal orders of participating states. These efforts revolve around the work of the Financial Stability Board, an organ of the G20 formally constituted in April 2009.[331] It serves three broad purposes. The first is to serve as a nexus point for the large group of economic regulatory agencies that exist at the national and international levels. The second is to generate information and data with respect to problems and policy approaches to national action. The third is to generate guidelines and other proto-regulation that could then serve as a legislative template for transposition into national legal orders. As reconstituted, the FSB was given a broad mandate, suitable for the overall coordination of economic policy and the generation of regulatory policy and frameworks.[332] To date it has produced three reports meant to lead to

329. *See generally*, Erik Holm, *Buffett Buys Goldman Stake in 'Economic Pearl Harbor'* (Update 2), BLOOMBERG.COM, Sept. 24, 2008, http://www.bloomberg.com/apps/news?pid=20601087&sid=aRef_DUx6AcU&refer=worldwide (last visited Dec. 20, 2009).

330. *Id.* "Billionaire Warren Buffett, calling turmoil in the markets an "economic Pearl Harbor," said his $5 billion investment in Goldman Sachs Group Inc. is an endorsement of the Treasury's $700 billion bank rescue plan. 'I am betting on the Congress doing the right thing for the American public and passing this bill,' Buffett said on cable channel CNBC today. 'I certainly have a vote of confidence in Goldman and vote of confidence in Congress.'" *Id.*

331. *See* FINANCIAL STABILITY BOARD, HISTORY, http://www.financialstabilityboard.org/about/history.htm (last visited Sept. 26, 2009). For the Financial Stability Board Charter, see http://www.financialstabilityboard.org/publications/r_090925d.pdf (last visited Sept. 26, 2009).

332. *Id.* at art. 2.

harmonizing regulation to be implemented at the state level.[333]

But the critical differences between these efforts and those of Norway's funds are important. They suggest the core regulatory framework issues that tend to be ignored in the rush to fit SWF regulation within conventional forms. Unlike investment activity, whether private or public, regulatory or participatory, sovereign activity is generally undertaken within the territory under the sovereign's control. The more attenuated its control, the more attenuated the intervention. And within the sovereign territory of another state, intervention is at least conceptually problematic, though effected in one way or another. When a state acts as a participant within the territory in which its sovereign power is greatest, it may be impossible to separate the public from the private (regulatory rather than participatory) functions of the state. That has been the position of the Europeans.[334] The U.S., on the other hand, has embraced the idea that such distinctions can, indeed, be made.[335] But Norway is not intervening in its own economy—it is projecting economic power abroad. And Norway is not seeking to extend its governmental power directly. It is protecting its wealth abroad like other private investors. But its objectives are its own. And the effects of its activities, whatever their form, may be distinctly felt. Moreover, the Norwegian state may be counting on that, so that the form of private investment is meant to mask the reality of political activity abroad.

And thus we come to the irony of regulatory approaches to sovereign wealth fund activities. The thrust of regulatory efforts neither reflect the realities of private fund behavior, nor the international regulatory consensus on the imposition of public obligations on private actors. In effect, the current approaches to SWF regulations appear to work at cross purposes with the current approaches to transnational regulation of private economic actors. The imposition of an idealized private investor model has the effect of forcing SWFs to act in a way that is substantially narrower than private investment entities. At the same

333. FINANCIAL STABILITY BOARD, IMPROVING FINANCIAL REGULATION (2009), http://www.financialstabilityboard.org/publications/r_090925b.pdf; FINANCIAL STABILITY BOARD, OVERVIEW OF PROGRESS IN IMPLEMENTING THE LONDON SUMMIT RECOMMENDATIONS FOR STRENGTHENING FINANCIAL STABILITY (2009), http://www.financialstabilityboard.org/publications/r_090925a.pdf; FINANCIAL STABILITY BOARD, FSB PRINCIPLES FOR SOUND COMPENSATION PRACTICES (2009) http://www.financialstabilityboard.org/publications/r_090925c.pdf.

334. *See* Backer, *supra* note 1, at 1847-50.

335. *See, e.g.*, Hughes v. Alexandria Scrap Corp., 426 U.S. 794 (1976); Wis. Dep't of Indus., Labor & Human Relations v. Gould Inc., 475 U.S. 282, 289 (1986); Reeves, Inc. v. Stake, 447 U.S. 429, 437 (1980).

time, the formally public/functionally private model suggests a division between public and private power that is belied by the reality of transnational regulatory behavior.

It is clear that the Norwegian Global SWF acts in a sovereign capacity. It deliberately seeks to project Norwegian policy preferences on a host of private actors otherwise beyond its reach. It seeks to use its investment strategies as a doorway to negotiate changes in foreign law, especially with respect to corporate social responsibility. But merely because Norway is pursuing sovereign objectives through its Global Fund and in private markets, and is doing so aggressively, does not mean that SWFs ought to be viewed as a threat any greater than large private investment vehicles that also aggressively intervene in regulatory matters. The issue ought to be the protection of the integrity of markets rather than the protection of taxonomy of public versus private market activity. As such, the object of reform ought to be the regulatory effect of interventions in private markets by public or private entities seeking to project power, rather than to bend public investment vehicles to a "private investor" model that does not even apply well to private investment funds. A framework of regulation focused in this way may provide a greater congruence between SWF regulation frameworks and those emerging in related fields, especially the regulation of multinational corporations.[336]

## VI. Conclusion

Sovereign wealth funds have become powerful players in the global economy. They are instrumentalities of the state without direct regulatory power. They appear to function like private pools of investment funds. But the character of their owner—states—have tended to complicate regulatory approaches to their operations within the territory of other states. This article has explored the contours of some of those issues. It has suggested that while sovereign wealth funds do function like private funds, they may pursue wealth maximization strategies different from those of private investors. If one holds a broad view of regulation, including all direct and indirect actions with regulatory effect, then sovereign wealth funds can be seen as a powerful method of indirect regulation—regulation through participation in private mar-

336. *See, e.g.*, Simon Chesterman, *The Turn to Ethics: Disinvestment from Multinational Corporations for Human Rights Violations—The Case of Norway's Sovereign Wealth Fund*, 23 American U. Int'l L. Rev. 577, 577-615 (2008) (considering the effectiveness of the Norwegian ethics scheme to regulate the behavior of multinational corporations along ethical lines).

kets. It provides a vehicle for extraterritorial application of municipal law impossible to effect directly. The antidote to this regulatory possibility is the creation of idealized private investors. The effect, of course, is to substantially circumscribe the power of states as states. Yet private individuals and large multinational corporations may act for the same indirect regulatory purposes of states—to increase their influence within states and among economic enterprises within those states that may increase their power in those territories.

The Norwegian sovereign wealth funds evidence the complexities of any simpleminded regulatory approach to the regulation of sovereign wealth funds. At one level, the funds act no differently than other private participatory funds. And that provides a strong argument in favor of little special regulation—a position taken by many influential academics in the United States and Europe. On the other hand, the macroeconomic and ethics based actions of the funds suggest that Norway is consciously pursuing state policy indirectly through its funds. Investment is clearly meant to project Norway's political power by other means, and to move policy in particular directions. That suggests a regulatory aspect to fund activity that belies that more benign characterization of fund activities at the heart of soft law efforts like the Santiago Principles. This was very much the case with respect to corporate social responsibility issues, where the examination focused on three actions—the implementation of responsible investor notions, the effectuation of a boycott of Israel through investment policy, and a reaction to the political situation in Myanmar through investment determinations.[337] But it was also evident from an examination of the Global Fund's responses to the financial crisis that there was a shift of investment inward and the use of the fund (through adjustment of diversification rules) to aid hard hit developing states through investment decisions.[338] Each of these represents a deviation from a model of indifferent private investment behavior norms, posited as fundamental to the treatment of sovereign investors like their private counterparts.

Ultimately the foundational issue touches on the increasing merger of public and private law. Multinational corporations now regulate and may be subject to public law obligations.[339] States may participate in markets and are entitled to the privileges of the market.[340] The easy

337. *See* discussion *supra* Section IV.A.

338. *See* discussion *supra* Section IV.B.

339. *See* Backer, *Rights and Accountability*, *supra* note 36; *See also U.K. NCP Statement*, *supra* note 37; *Final statement*, *supra* note 37.

340. *See* Kimmitt, *supra* note 4.

separation of economic and political activity is now more difficult. Regulatory frameworks will have to reflect this complexity as well.

The Norwegian SWF suggests the contours of what is emerging as an influential model of SWF governance and its contradictions grounded in this amalgamation of public and private law regimes. On the one hand, the "model" SWF, reflected in part by the Norwegian SWF, embraces that assumption that a public entity can organize itself to act like a private entity in the markets of host states. It also suggests the parameters of "model" private conduct. The "reward" for adhering to this model is the promise of host states to refrain from enacting protectionist measures—that is, to accord state investment vehicles substantially the same treatment accorded to similar private entities. Yet, this sort of state organization, formally public but functionally private, does not reflect the reality of private investor behavior, who seek to use investment for political ends. Neither does this model of SWF governance realistically limit the ability of state investment entities to project political power through market investment strategies, even when these entities purport to refrain from that sort of activity.[341] These contradictions will remain unresolved, and consequently regulatory frameworks remain ineffective, until a regulatory framework emerges that recognizes that private entities engage in commercial activity for political purposes and that states' economic activities can be substantially separated from its public policy objectives.

341. *See* Philip Whyte & Katinka Barysch, *What should Europe do about sovereign wealth funds?*, CENTRE FOR EUROPEAN REFORM BULLETIN (Oct./Nov. 2007), *available at* http://www.cer.org.uk/articles/56_whyte_barysch.html (last visited Mar. 30, 2009) ("Even if SWFs tried to buy majority stakes, it is not clear that host countries should necessarily prevent them from doing so. After all, state-owned companies have been allowed to make cross-border takeovers within the EU: Electricité de France entered the UK's liberalised energy market by acquiring a handful of companies already competing in it. In most cases, a host country's response to a mooted takeover by an SWF should be confined to ensuring that it poses no threat to domestic competition.").