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Competitive Third-Party Regulation:

How Private Certification Can Overcome Constraints that Frustrate Government Regulation

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Abstract

Private certification as a means of risk regulation and quality assurance offers advantages over government regulation, including superior technical expertise, better inspection and monitoring of regulated entities, increased responsiveness to consumers, and greater efficiency. This article examines two examples of reliable private certification in regulatory arenas—fire safety and kosher food—where political opposition and resource constraints have frustrated government regulatory efforts. The article identifies the conditions that promote reliable private certification and analyzes its comparative institutional advantages over government regulation. Critics of private certification question its legitimacy, asserting that private regulation is less participatory, transparent, and accountable than government regulation. The article responds to these claims, arguing that the two examples of private certification presented here compare favorably with government regulation based on these criteria of legitimacy.

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Private certification as a means of risk regulation and quality assurance is widespread. A *Directory of U.S. Private Sector Product Certification Programs* published in 2001 by the Department of Commerce lists 180 nongovernmental organizations based in the U.S. that certify more than 850 types of products—ranging from adhesives, bananas, and cabinets to valves, weatherproofing, and yachts. These private entities provide assurance that the products they certify meet criteria specified by professional associations, standards organizations, and government agencies.[1] Private certification extends beyond products to include professional services, such as dentistry and financial management, as well as institutions, such as hospitals and universities.[2] Consumers count on private certification when they purchase goods and services; companies rely on it when obtaining inputs and choosing suppliers, and government agencies use it to assess regulatory compliance.[3] Private certification has developed into an industry in its own right, complete with trade associations, professional standards, and accreditation to provide quality assurance of certification services.[4]

In many instances, private certification transcends limits that hamper government regulation. Key to its success is market demand. Whereas government frequently lacks resources to develop, implement, and enforce regulations, private certification can generate fees to cover these costs. Moreover, industries that resist government oversight are often willing to pay for private certification to enhance the value of their products and services.

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[1] Robert B. Toth, *Standards Activities of Organizations in the United States* 4, 290-303, 307-338 (National Institute of Standards and Technology, U.S. Dept. of Commerce, 1991).
[2] See, e.g., *The Mission of the American Board of General Dentistry*, http://www.abgd.org/mission.php (accessed 4/28/13); *Certified Financial Manager*, http://accounting.smartpros.com/x12791.xml (accessed 4/28/13); *About the Joint Commission*, http://www.jointcommission.org/about_us/about_the_joint_commission_main.aspx (accessed 4/28/13); *Council for Higher Education Accreditation*, http://www.chea.org/public_info/index.asp (accessed 4/28/13).
[3] Lesley K. McAllister, *Regulation by Third-Party Verification*, 53 B.C. L. REV. 1 (2012).
[4] Lesley K. McAllister, *Third-Party Programs to Assess Regulatory Compliance* (Administrative Conference of the United States, Revised Draft, Oct. 5, 2012).

Unfortunately, private certification is not always reliable. Market competition among certifiers sometimes leads them to lower their standards in order to reduce the cost of their services and ease the demands that they place on their clients. The result is a race to the bottom. For example, a congressional panel accused credit rating agencies of issuing favorable assessments of mortgage-backed securities that proved to be worthless, calling the agencies an "essential cog in the wheel of financial destruction."[5] In another notorious example, a private food safety auditing firm awarded the Peanut Corporation of America a "superior" rating shortly before the company's products caused a nationwide salmonella outbreak that killed nine people and sickened over 22,000. Following the outbreak, federal inspectors found dead rodents, open holes in the roof, and pools of stagnant water at two production facilities. "'Superior' clearly doesn't mean much," quipped one congressman, "How many dead mice do you have to find in your food before you get an 'Excellent' rating?"[6]

Reliable private certification harnesses market demand for certification without succumbing to competitive pressures to cut corners. This article examines two examples of reliable private certification in regulatory arenas—fire safety and kosher food—where political opposition and resource constraints have frustrated government regulatory efforts. These examples highlight some of the comparative advantages of private certification over government regulation. They also provide insights into how private certifiers can resist pressures to lower standards in ways that undermine their reliability.

[5] *Conclusions of the Financial Crisis Inquiry Commission* xxv, at http://fcic-static.law.stanford.edu/cdn_media/fcic-reports/fcic_final_report_conclusions.pdf (accessed 4/28/13).
[6] Elizabeth Weisse, *Food Safety Auditors Are Often Paid by the Firms They Audit*," USA TODAY, Oct. 4, 2010, at http://usatoday30.usatoday.com/money/industries/food/2010-10-01-foodaudits01_ST_N.htm (accessed 4/28/13).

Private certification is part of a complex array of related and overlapping regulatory instruments, which includes standard setting, testing, inspection, and accreditation.[7] This article focuses specifically on *certification*, by which I mean attesting that a product, service, or institution conforms to a specified standard. Moreover, although various public and private institutions provide certification, this article examines *third-party* certification, meaning certification by entities other than those that make the products, provide the services, or operate the institutions being certified (first party-certification), or that consume or use them (second-party certification). In addition, my two examples illustrate certification by *private* entities rather than by government agencies. And finally, the two examples are *self-regulating*, meaning that they are not subject to government oversight. In sum, the article identifies conditions that support reliable *self-regulating private third-party certification*, and analyzes its comparative institutional advantages over administrative regulation by government agencies. I will use the shorthand "private certification" to refer to this regulatory instrument.

To describe private certification as an alternative to government regulation oversimplifies the variety of possible relationships between them. Sometimes, private certification fills a void where government is unwilling or unable to regulate. Other times, private certification merely fills gaps in an area where government regulation operates but is not comprehensive. Private certification may complement or compete with government regulation. The two may be mutually reinforcing or redundant. Moreover, the relationship between them need not be static; it may change over time.[8] This article does not attempt to map the full spectrum of possibilities. More

[7] Maureen A. Breitenberg, *The ABC's of the U.S. Conformity Assessment System* (National Institute of Standards and Technology, U.S. Dept. of Commerce, 1997); McAllister, *Regulation by Third-Party Verification*, supra note ?; McAllister, *Third-Party Programs*, supra note ?; Yesim Yilmaz, *Private Regulation: A Real Alternative for Regulatory Reform*, POLICY ANALYSIS, April 20, 1998, http://www.cato.org/sites/cato.org/files/pubs/pdf/pa-303.pdf.
[8] ROSS E. CHEIT, SETTING SAFETY STANDARDS 173-4 (1990).

modestly, Part I presents two examples of reliable private certification that overcame obstacles that frustrated government regulation.

As the failures of private certification demonstrate, market incentives can be a source of poor performance. Part II analyzes how the two examples of private certification presented in Part I overcame incentives to put profits ahead of protecting the public. One sees in these examples how brand competition, professionalism, bureaucratic controls, a shared sense of mission, and social networks support reliable private certification.

Two examples, of course, do not support a general preference for private over public regulation. They do, however, illustrate several comparative institutional advantages of private certification. Part III surveys these advantages.

Even when private regulation performs well, critics question its legitimacy, asserting that private regulation is less participatory, transparent, and accountable than government regulation.[9] Part IV addresses these claims, arguing that the two examples of private certification presented here compare favorably with government regulation based on these criteria of legitimacy.

I. Two Examples of Private Certification

Private certification can provide reliable information to consumers and incentive for certified entities to improve the safety and/or quality of their products, services, or institutions. Fire safety and kosher food certification exemplify these benefits of private certification. Detailed analysis of these two examples, however, is beyond the scope of this article. The descriptions presented here are merely schematic, and readers seeking more complete accounts should consult the sources cited in the footnotes.

[9] Doris Fuchs, Agni Kalfagianni, and Tetty Havinga, *Actors in Private Food Governance: The Legitimacy of Retail Standards and Multistakeholder Initiatives with Civil Society Participation*," AGRICULTURE & HUMAN VALUES (Aug. 13, 2009), springerlink.com (accessed 4/28/13).

A. Fire Safety

In a period of devastation that became known as the "Conflagration Era," fires ravaged American cities throughout the late nineteenth and early twentieth centuries. The Great Chicago fire of 1871 destroyed more than 17,000 buildings and killed 250 people. Total damage was estimated at $196 million ($3.7 billion in 2012 dollars). Cities from Boston to Seattle endured fires on a similar scale. In the wake of these disasters, government attempts to improve fire safety were consistently hampered by short public attention spans and active political opposition from powerful developers and ordinary citizens eager to keep building costs down. Resource constraints and limited expertise further frustrated government efforts. Fire risk varied unpredictably from building to building in rapidly changing urban environments, and effective policies required extensive information gathering, sophisticated standards development, and vigilant compliance monitoring—all of which were beyond the government's capacity.[10]

Seeking ways to more accurately price risk and reduce losses, insurance companies organized industry associations to develop expertise in fire safety. They investigated fires to determine what caused them and sponsored laboratory research to analyze building materials and firefighting equipment. Underwriters also devised fire safety standards, conditioned coverage on adherence to them, and conducted routine inspections of buildings covered by their policies.[11] As part of these efforts, William Henry Merrill, an MIT-educated engineer, obtained funding in 1895 from the National Board of Fire Underwriters to conduct fire safety testing on building materials and electrical appliances. In that year, Merrill and his small staff completed 75 tests on a $3000 budget. Two years later, he published a list of "approved fittings and electrical devices,"

[10] This account of the history of urban fires and government responses relies on SCOTT G. KNOWLES, THE DISASTER EXPERTS: MASTERING RISK IN MODERN AMERICA 21-37, 45, 69, 71, 84, 108, 111-112 (2011).
[11] *Id*. at chs. 1-2.

which he distributed to fire underwriters and municipal fire service officers. The operation was incorporated in 1901 under the name Underwriters Laboratories (UL).[12]

UL grew rapidly. By 1905, it had published 75,000 reports on building materials and electrical appliances, and its annual budget was $300,000.[13] It became financially independent in 1916, relying exclusively on fees from manufacturers for its services, which included product testing, factory inspection, and labeling.[14] 50 million products carried the UL label in 1915, a number that grew to 500 million by 1922.[15] In the late 1920s, more than 200 UL engineers staffed regional laboratories in Chicago, New York, and San Francisco, and UL employed 250 inspectors operating out of offices in 141 American cities and London.[16]

The demand for fire safety certification was fueled by insurance companies, local governments, the construction industry, manufacturers, and consumers.[17] UL encouraged this demand by aggressively marketing fire safety. Fire safety certification increased the value of products, and UL executives traveled the country to convince manufacturers to label more and more of them.[18] These UL executives preached a gospel of fire safety in speaking tours, popular magazines, professional journals, books, radio, and movies. As part of these public education efforts, they conducted regular tours of their laboratories for professionals and the general public.[19]

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[12] *Id.* at 50-56; NORM BEZANE, THIS INVENTIVE CENTURY: THE INCREDIBLE JOURNEY OF UNDERWRITERS LABORATORIES 9, 47 (1994); Knowles speculates that these reports were also available to anyone who wrote to request one. Email from Scott G.Knowles, July 24, 2013 (on file with author).
[13] BEZANE, *surpa* note ?, at 9.
[14] KNOWLES, *supra* note ?, at114; BEZANE, *supra* note ?, at 48.
[15] KNOWLES, *supra* note ?, at 122.
[16] *Id*. at 129; BEZANE, *supra* note ?, at 13.
[17] KNOWLES, *supra* note ?, at at 122, 127, 129.
[18] Scott G. Knowles, *Inventing Safety: Fire, Technology, and Trust in Modern America*, 209 (unpubl. PhD diss., 2003).
[19] KNOWLES, DISASTER EXPERTS, *surpa* note ?, at 111-114, 117-119, 124, 138; Knowles, *Inventing Safety*, *surpa* note ?, at 173, 250.

Under Merrill's leadership, UL successfully branded its services as the most reliable in fire safety certification and established itself as the industry leader. Fire insurance companies conditioned coverage on the use of UL-approved building materials.[20] Local governments incorporated UL standards into their building codes.[21] Manufacturers relied on UL testing to develop their products, and they touted UL approval in their marketing to consumers, who increasingly demanded assurances of fire safety and came to recognize the UL label.[22]

To support UL's brand, Merrill set high standards for expertise and professionalism. He hired laboratory personnel with engineering degrees from leading technical colleges and universities. UL partnered with the Armour Institute in Chicago to develop a new degree in Fire Protection Engineering, providing practical training to students in UL laboratories as part of their studies. The rise of engineering in general, and fire protection engineering in particular, distinguished UL's professional scientists from tradesmen and mechanics.[23] Merrill further cultivated expertise among his engineering staff by organizing testing operations into specialized departments, such as electrical, chemical, gases and oils, and hydraulic.[24] Merrill also set high professional standards for UL inspectors. He favored hiring inspectors with practical experience in fire protection.[25] He insisted that they employ "integrity, tact, and a goodly amount of common sense" in their relationships with clients so that they could obtain sufficient information to discover mistakes or misconduct that could result in substandard products.[26] Merrill emphasized professional ethics, prohibiting UL personnel from accepting gifts from clients."[27]

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[20] KNOWLES, DISASTER EXPERTS, *supra* note ?, at 120-121; Knowles, *Inventing Safety*, *supra* note ?, at 185.
[21] KNOWLES, DISASTER EXPERTS, *supra* note ?, at 129-140.
[22] *Id*. at 116-117, 122, 138, 122-123, 128-129 (manufacturers' reliance on UL testing for product development), 118 (consumer demand for assurance of fire safety); Knowles, *Inventing Safety*, *supra* note ?, at 185.
[23] Knowles, *Inventing Safety*, *supra* note ?, at 122-138; KNOWLES, DISASTER EXPERTS, *supra* note ?, at 128.
[24] Knowles, *Inventing Safety*, *supra* note ?, at 184; KNOWLES, DISASTER EXPERTS, *supra* note ?, at 130.
[25] KNOWLES, DISASTER EXPERTS, *supra* note ?, at 128.
[26] *Id*. at 121
[27] *Id*. at 117, 131

Merrill also built up UL's reputation for reliability by creating organizational structures, administrative routines, and oversight systems designed to prevent mistakes and misconduct. In 1916, Merrill ended UL's financial dependence on the insurance industry, incorporating as an independent organization.[28] To ensure the integrity of its testing process, UL charged the same testing fees for products that failed as for those that passed.[29] UL field inspectors were supervised by central office engineers.[30] In larger regions, field inspectors were rotated among different routes to avoid "unconscious carelessness."[31] All product tests and factory inspections were carefully documented in standardized reports that were printed and maintained in files at UL offices, and printed cards recording product certifications were distributed to insurance companies and government agencies.[32] To provide an independent review of its testing results, UL established oversight councils composed of "men without commercial interest in the devices covered in reports submitted for their review," including insurance representatives and engineers from government agencies, such as the National Bureau of Standards. UL test results required approval by the relevant oversight council, and manufacturing clients received reports detailing the basis for their decision.[33] Three other organizations with significant fire safety expertise—the Underwriters' National Electric Association, the National Board of Fire Underwriters, and the National Fire Protection Association—exercised additional oversight as major stockholders in UL.[34] UL also routinely submitted its safety standards to the American National Standards Institute (ANSI) for recognition as nationally recognized consensus standards, a process that

[28] *Id.* at 114
[29] *Id.* at 116
[30] *Id.* at 121, 128
[31] *Id.* at 121
[32] *Id.* at 117-118, 121, 149.
[33] *Id.* at 131; Knowles, *Inventing Safety*, *surpa* note ?, at 204, HARRY CHASE BREARLEY, A SYMBOL OF SAFETY: AN INTERPRETATIVE STUDY OF A NOTABLE INSTITUTION ORGANIZED FOR SERVICE—NOT PROFIT 255 (1923).
[34] KNOWLES, DISASTER EXPERTS, *supra* note ?, at 131; Knowles, *Inventing Safety*, *supra* note ?, at 205.

involved soliciting public comments on the standards through a notice in the UL newsletter, *Standards Action*.[35]

Aside from professionalization and bureaucratic controls, Merrill nurtured a strong sense of mission that pervaded the organization from top management to engineers and inspectors. "The fact that we are working for a common end, and that this end is to benefit humanity, not enrich a class or an individual, is in itself an inspiration," wrote one UL employee in 1920, reflecting a mix of corporate pride and reform zeal.[36] Such "anti-combustion missionaries," as many fire safety professionals described themselves, took jobs at UL that paid less than comparable work elsewhere, and they stayed.[37] Merrill emphasized UL's nonprofit character, although he was well aware that successful branding and marketing to obtain paying clients were essential to UL's independence and sustainability.[38]

Competition for clients among independent testing labs and the proliferation of rival services provided by underwriters' organizations, fire officials, and urban safety councils made UL highly brand sensitive.[39] The company quickly responded to criticisms of its certification with investigations to clear up misunderstandings or correct mistakes.[40] It also sought to build its reputation for trustworthiness through transparency—sharing complete reports of its decisionmaking with industrial clients, publishing lists of approved products, and inviting the public into its facilities to observe its testing procedures.[41]

In promoting itself as uniquely qualified and unrivaled in its expertise, UL gained a level of market dominance that opened it to charges of monopoly. While denying any effort to restrict

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[35] CHEIT, *supra* note ?, at 98.
[36] KNOWLES, DISASTER EXPERTS, *supra* note ?, at 126.
[37] *Id.* at 126.
[38] *Id.* at 148-149.
[39] KNOWLES, DISASTER EXPERTS, *supra* note ?, at 149; Knowles, *Inventing Safety*, *supra* note ?, at 236-237. See also CHEIT, *supra* note ?, at 108-9.
[40] *Id.* at 151-2.
[41] KNOWLES, DISASTER EXPERTS, *supra* note ?, at 149.

competition, UL insisted that its dominance was based on the superior quality of its work and the purity of its motives. "A claim of monopoly in our work can be justified," argued a 1922 article in its magazine, "so long as none other is equally competent in technique, in experience, in facilities, and in sincerity of our motives."[42] In criticizing its competitors, UL insisted that it had "an obligation to state our earnest opposition to the activities of individuals, organizations, commissions, or similar bodies engaged in the classification of firefighting equipment except that the motives, the ability, facilities and other most necessary equipment is available and skillfully employed."[43]

UL's participation in a network of fire safety institutions provided peer pressure to maintain high standards and disseminated reputational information among opinion leaders. For example, by World War II, UL personnel participated in over 100 National Fire Protection Association (NFPA) committees composed of fire service professionals, state and local fire safety officials, representatives of the building trades and industry groups, academic researchers, and fire insurance engineers. These committees, and others like them, comprise the consensus code system which promulgates voluntary standards that are typically adopted by government agencies and private industry.[44] The network is also characterized by frequent collaborations between private standards and testing organizations such as UL and the American Society for Testing and Materials (ASTM), industry associations such as the National Board of Fire Underwriters (NFBU), and government agencies such as the National Bureau of Standards

[42] Since establishing itself as a market leader, UL has successfully defended itself against antitrust allegations. In 1943, however, a federal court denied UL's tax-exempt status as a 501(c)(3) organization, in response to which Congress passed legislation in 1954 amending section 501(c)(3) to include "testing for public safety," thereby restoring UL's tax-exempt status. *Id*. at 157-160.
[43] *Id*. at 149-150.
[44] *Id*. at 129-140.

(NBS) (now the National Institute of Standards and Technology, or NIST) and the US War Department (now the Department of Defense).[45]

Today UL remains the market leader in fire safety certification, as well as in many other areas of product testing. It currently certifies more than 20,000 different types of products for 69,000 manufacturers, and its safety logo appears on 22 billion items worldwide.[46] The company estimates that the average American home contains 125 UL markings.[47] The regulatory landscape in fire safety has become quite complex, inhabited by a wide array of private firms, industry associations, and government agencies.[48] My simplified account and emphasis on UL's formative years is designed to highlight the features of private certification that account for its success, the subject of Part II, and its comparative institutional advantages over government regulation, which I will discuss in Part III.

[45] KNOWLES, DISASTER EXPERTS, *supra* note ?, at 134-136, 139.
[46] *By the Numbers*, http://www.ul.com/global/eng/pages/aboutul/whatwedo/bythenumbers/ (accessed 4/29/13).
[47] Julie Wernau, More than a Label: Underwriters Laboratories Looks to Expand Its Reach, Adding Products and Countries Too, Chicago Trib., June 29, 2011, http://articles.chicagotribune.com/2011-06-29/business/ct-biz-0630-underwriters-20110629_1_william-henry-merrill-john-drengenberg-electrical-safety (accessed 4/29/13).
[48] *International Building Code*, WIKIPEDIA, http://en.wikipedia.org/w/index.php?title=International_Building_Code&oldid=563808066 (accessed 7/22/13).

B. Kosher Food

At the turn of the twentieth century, kosher meat production was notorious for scandals involving price fixing, racketeering, and even murder-for-hire. The New York City Department of Markets estimated in 1925 that 40 percent of the meat sold as kosher in the city was not kosher. Industry associations and consumer advocates estimated the rate between 50 and 65 percent. [49]

The traditional means of regulating kosher trade in the Old World had been centralized communal control backed by government power. Local community councils possessed legal authority to issue exclusive licenses to slaughter and sell kosher meat within their jurisdictions. But religious voluntarism and free markets in America rendered this approach unworkable. By the mid-1800s, most Jewish communities in America contained a diverse mix of immigrants from different cultural backgrounds who founded rival synagogues within the same locality. Individuals could easily disregard the directives of congregational authorities by simply joining another synagogue, or founding a new one. Moreover, in America, Jewish communal authority was not an extension of civil government, and community leaders had no coercive power to enforce uniform kosher standards or to restrict the sale of goods. The problem of kosher fraud was too big for government regulators. Six full-time kosher inspectors in the New York City Department of Markets and ten in the New York State Kosher Enforcement Bureau by the late 1930s were insufficient to oversee the 18,000 kosher food establishments in New York City.

Reform finally came to the American kosher food industry with increasing demand among kosher consumers for industrially produced canned and packaged foods and the rise of private kosher certification agencies. Packaged foods presented new opportunities for kosher certifiers

[49] This paragraph and the next rely on TIMOTHY D. LYTTON, KOSHER: PRIVATE REGULATION IN THE AGE OF INDUSTRIAL FOOD Intro. & ch. 1 (2013).

outside of kosher meat production, and they changed the economics of kosher certification. Meat production is labor intensive and, therefore, relatively slow. Kosher meat production additionally requires a specially trained slaughterer, on-site rabbinic oversight, and supervision of the meat from the moment of slaughter to the time of sale. The resulting high unit cost of producing kosher meat led many slaughterhouses and retail butchers to fraudulently substitute nonkosher meat for kosher meat while still charging the premium for kosher meat. Since nothing in the appearance of the meat testified to its kosher status, fraud was difficult to detect. By contrast, kosher certification of industrially manufactured packaged foods generally requires an initial inspection of the production facility and periodic inspections that range from weekly to annual, depending upon the nature of the production. Given the fast rate of industrial production, these costs are typically spread across tens, or even hundreds, of thousands of production units. This lower unit cost greatly reduced incentives for fraud.[50]

Kosher certifiers aggressively marketed their services to food manufacturers as a low-cost, highly effective marketing strategy. This effort was pioneered by Rabbi Alexander Rosenberg, the "guru" of kosher marketing, who assumed leadership of the Orthodox Union (OU) kosher certification service in 1950. Rosenberg explained to leading food industry executives that kosher consumers were a small but highly influential demographic because they were concentrated disproportionately in major metropolitan markets. By increasing a company's market share in those major markets, the company's products would achieve better positioning on store shelves, where all consumers, not just kosher consumers, would be more likely to see and buy them. A marketing manager at Duncan Hines recalls that Rosenberg taught him that "the whole grocery business depends upon shelf space." As a result of OU certification, according to

[50] *Id.*

the manager, sales to the company's cake mix among ordinary consumers rose 40 percent in two months.[51]

Under Rosenberg's leadership, the OU experienced sustained and dramatic expansion of its certification services. In 1945, the OU employed 40 kosher supervisors to certify 184 products for 37 companies. By 1970, near the end of Rosenberg's tenure, the OU employed more than 750 supervisors to certify in excess of 2,500 products for 475 companies. During this time, the OU established itself as the largest and most widely-known kosher certifier, a position that it still occupies today.[52]

Rosenberg created a brand to distinguish OU certification from its competitors, individual rabbis who typically provided kosher certification as a way to supplement meager congregational salaries. Rosenberg argued that these rabbis lacked sufficient expertise in Jewish dietary laws and had a conflict of interest insofar as they were paid directly by the companies that they certified. By contrast, the OU presented itself as a nonprofit organization staffed by specialists who received fixed salaries regardless of whether the products submitted to their review received certification or not. Rosenberg believed that having a company pay the OU central office for certification services provided by one of its salaried rabbis rather than paying a local freelance rabbi directly would lessen the conflict of interest that a rabbi might feel to lower his standards in order to approve the company's product. In his discussions with company executives, Rosenberg touted the OU's reputation among kosher consumers as maintaining "the highest *Halachic* [Jewish law] standards" and as the only kosher certification "free of private interest." Whereas kosher certification of products by private rabbis was publicized by word of mouth or signified

[51] *Id*. at ch. 2, the quote is at 47.
[52] *Id*. at 46-47, 74-81.

by a generic "K" on the package, OU-certified products carried the organization's distinctive Ⓤ symbol.[53]

The OU backed its reputation for reliable kosher supervision by replacing the freelancing private congregational rabbi with an organization staffed by a new breed of highly trained kosher professionals. Rosenberg initiated this process of professionalization, but it was developed much more fully after his departure by Rabbi Menachem Genack, who assumed leadership of the OU in 1980. By that time, a number of competitors began to emulate the OU, and, in the competition for clients, influenced the OU's own development. Today, the OU and these other agencies train their personnel not only in Jewish dietary laws but also in food chemistry, food technology, customer relations, and professional ethics. The larger agencies produce a steady flow of lectures, conferences, workshops, newsletters , magazines, scholarly journals, books, and videos that support initial training and ongoing professional education. Kosher inspectors must pass a test, attend educational programming, and keep up with the relevant literature. They must have a thorough familiarity with the raw materials, food chemistry, and processing equipment used in the plants they oversee. Agency personnel increasingly specialize in certain types of food processing, such as baked goods, beverages, botanicals, candy, dairy, dressings and sauces, eggs, emulsifiers and enzymes, fish, flavors, meat, nuts, oils, oleochemicals, Passover, pasta, pickles, potatoes, powdered goods, soy, spices, vegetables, vitamins, and wine or in geographic regions where production takes place, such as Europe, Israel, and the Far East.[54] To avoid even the appearance of impropriety, agencies prohibit inspectors from accepting gifts from clients.[55]

Led by the OU, the new breed of kosher certification agencies also changed the organizational structure and administrative practices of kosher certification in ways designed to

[53] *Id*. at 48.
[54] *Id*. at 63-64.
[55] *Id*. at 50.

prevent mistakes and deter misconduct. The agencies separated decisions about kosher standards from business development by entrusting the former to independent rabbinic experts and the latter to rabbinic administrators. They also instituted new systems of management oversight. For example, at the OU, kosher inspectors in the field are supervised by rabbinic coordinators, who answer to a top management team led by a rabbinic administrator, who, in turn, is accountable to a board of directors. Since the mid-1980s, agencies have computerized their record keeping, creating huge databases including records of hundreds of thousands of ingredients, allowing the agencies to track down erroneously certified items and remove them quickly from production.[56]

Religious commitment has contributed to better management oversight and greater professionalism within kosher certification agencies. Many religious Jews believe that consumption of nonkosher food, even by mistake, irreversibly contaminates one's soul and interferes with one's capacity to connect to God. Causing another Jew to consume nonkosher food is considered a grievous sin. Consequently, each agency seeks to cultivate among its personnel a religious commitment to the agency's goal of making reliably kosher-certified foods widely available and affordable.[57]

In the fierce competition for industrial clients, the leading kosher certification agencies are highly brand sensitive. They solicit consumer feedback and respond to concerns through their public presentations, telephone hotlines, websites, newsletters, and magazines.[58] Agencies also routinely publish alerts and order recalls when they discover problems. "They don't look so great when they do this, but they are doing it on a regular basis," asserts one kosher industry expert. "No day goes by without a consumer alert issued by one of the major [kosher certification] organizations saying 'this has been mislabeled,' or 'this is not kosher'. . . . There is a constant

[56] *Id*. at 62-68.
[57] *Id*. at 65-66.
[58] *Id*. at 116.

stream of 'fessing up, if you will." Regular disclosure of problems to consumers is essential to maintaining agency brand value. "It enhances their credibility when they are honest," explains the expert. Consumers "know that mistakes happen, and, as long as they see that you are actually telling people when you make a mistake, it gives greater credibility to the [kosher supervision]."[59]

A trade association—the Association of *Kashrus* Organizations (AKO), founded in 1985—provides a venue for exchanging information, setting uniform industry standards, and alerting agencies about certifiers who fall below these standards.[60] Reputational information about agencies is passed along to consumers through alerts in agency publications and websites, and further disseminated through social networks, especially among a core of the most religiously observant kosher consumers.[61]

Today, kosher food is big business. More than 10,000 kosher-producing companies operate in the United States alone, making more than 135,000 retail kosher products for over 12 million American consumers who purchase kosher food because it is kosher. Only 8 percent of kosher consumers are religious Jews—the rest choose kosher food for reasons related to health, food safety, taste, vegetarianism, and lactose intolerance or to satisfy non-Jewish religious requirements such as *halal*. The U.S. kosher market generates more than $12 billion in annual retail sales, and more products are labeled kosher than are labeled organic, natural, or premium.[62]

Although there are more than 300 kosher certification agencies, the industry is governed by the five largest agencies, collectively known as the "Big Five." Within this group, the OU is by

[59] *Id*. at 108-109.
[60] *Id*. at 91-97. The term *kashrus* is Hebrew for kosher dietary restrictions.
[61] *Id*. at 133-134.
[62] *Id*. at 3.

far the largest agency in terms of number of company clients, plants supervised, products certified, and staff size. The OU certifies more than twice as many ingredients as its nearest competitor, and the OU symbol appears on more than two-thirds of all kosher-certified items in the supermarket—more than twice the number of all other symbols combined.[63] The OU's predominance generates some resentment among its rivals, as well as occasional charges of monopolistic behavior. Because certifiers are so interdependent, however, they mostly rise above such tensions in order to conduct business, maintain minimum standards, and avoid public displays of acrimony that would tarnish the image of the industry as a whole.[64]

C. Evaluating the Performance of Private Certification

Although UL and the OU exemplify successful private certification, they are not immune to criticism. At least one commentator has argued that some of UL's standards are too low because of inadequate investment in research.[65] Manufacturers complain that UL's standards are too high in order to favor some companies over others.[66] Similar charges are leveled against the OU. Some accuse the agency of cutting corners to save money and increase profits, while others allege that it is unnecessarily stringent so it can charge for unnecessary certification of products that do not require kosher certification.[67]

Assessing the performance of UL and the OU is complicated by the difficulty of constructing objective benchmarks by which to evaluate their standards. In the case of UL, one might subject its fire safety standards to cost-benefit analysis. But cost-benefit evaluations of fire safety standards are themselves not entirely objective—they rely heavily on rough estimates and

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[63] *Id*. at 74-79
[64] *Id*. at 64-65, 73, 99, 103, 159-160.
[65] CHEIT, *supra* note ?, at 106-109, 201.
[66] KNOWLES, DISASTER EXPERTS, *supra* note ?, at 153; CHEIT, *supra* note ?, at 107.
[67] LYTTON, KOSHER, *supra* note ?, at 104-105, 121-122.

speculation, since existing data is incomplete and additional data is expensive to collect. Indeed, UL itself performs cost-benefit analysis in developing standards, typically based on the most complete information available, and it is unclear that any other entity could produce a better cost-benefit analysis that could serve as a more objective benchmark.[68] In the case of the OU, kosher standards are the product of legal judgments that are subject to disagreement among rabbinic scholars, based on differences in their interpretation of legal sources and their religious policy preferences—all of which undermines the idea of objective kosher standards independent of particular rabbinic interpretive communities.[69] These difficulties of identifying benchmarks, challenging enough when evaluating an individual standard, are compounded when attempting to judge overall performance of a large organization like UL or the OU.

The most extensive studies of UL and the OU, while they do not overcome these difficulties, nevertheless conclude, relying on very general assessments, that UL and the OU have made significant contributions to reducing fire risk and kosher fraud respectively. Since this article focuses on what accounts for the success of private certification in these two regulatory arenas, I will rely on these general assessments, without offering any additional evidence or greater precision. Scott Gabriel Knowles, in his history of fire safety regulation from the mid-1800s to the mid-1900s, *Inventing Safety: Fire, Technology, and Trust in Modern America*, offers a lengthy assessment that demonstrates how UL led a new, professionalized fire safety industry in reducing the risk of fire posed by building materials and consumer products at a time when government lacked the expertise and political will to do so. When government finally did begin

[68] CHEIT, *supra* note?, at 106, 168-172 Alternatively, instead of assessing its standards directly, one might measure UL's standard-setting procedures against some ideal of administrative procedure. But, again, it is not clear how reliable such a benchmark would be, since any ideal of administrative procedure is likely to be either too abstract to provide a useful metric or controversial. Moreover, it is difficult to quantify procedural values such as accountability with much precision.

[69] See, e.g., LYTTON, KOSHER, *supra* note?, at 82-83, 104-105, 121-122.

to regulate fire safety at the end of this period, it generally adopted private standards developed by UL and other private organizations.[70] Ross Cheit, in *Setting Safety Standards: Regulation in the Public and Private Sectors*, analyzes several case studies of private standard setting in the 1970s and 1980s by UL and other organizations. Cheit concludes that, while the private safety standards he studied frequently relied more on educated guesses than rigorous scientific calculations, they were, for the most part, "within the zone of reasonableness," and when they were not, they more often were "overly strict" rather than "too lax."[71]

Moreover, Cheit asserts that UL certification of compliance with these standards is highly reliable. "The income received from [product testing], combined with the threat of liability if products do not actually meet the stated requirements, prompts the testing labs to implement comprehensive inspections schemes," asserts Cheit. "Testing labs go to extraordinary lengths to ensure that products bearing their label comply with their standards."[72]

In *Kosher: Private Regulation in the Age of Industrial Food*, I present evidence that "industrial kosher certification has overcome the widespread fraud and corruption that characterized kosher meat production in the early decades of the twentieth century."[73] While no objective measure of kosher standards is possible, I conclude that most agencies adhere to common standards determined by deliberation among leading agencies, foremost among them the OU, and that these standards coincide with the preferences of the roughly 10 percent of kosher consumers who have a high level of Jewish observance and have opinions on standards. Moreover, some certification agencies employ standards that deviate from these common

[70] Knowles, *Inventing Safety*, *supra* note ?. See also, KNOWLES, DISASTER EXPERTS, *supra* note?, at chs. 1-3.
[71] CHEIT, *supra* note?, at 100-106 (check), 172.
[72] *Id*. at 183. For examples of certifier liability for negligence, see Peter H. Schuck, *Tort Liability to Those Injured by Negligent Accreditation Decisions*, 57 L. & CONTEMP. PROBS. 185, 192 (1994).
[73] LYTTON, *supra* note?, at 106-111.

standards—some more lenient and others more stringent—in order to respond to consumers outside the religious mainstream.[74]

Available evidence suggests that kosher agency certification of compliance with these standards is highly reliable. To begin with, self-reported agency data suggests that the rate of erroneous certification is very low. For example, of the half-million products that the OU certifies each year, its legal department investigates only about five hundred cases of questionable use of the OU symbol, and it takes action in only fifty of those cases. Data from other leading kosher certifiers reflect a similarly low rate of erroneous certification. Agencies' routine disclosure of these cases of erroneous certification—at significant cost to the agencies and their food-company clients—bolsters the credibility of this self-reported data. Each of the major agencies posts on its website several alerts every month warning consumers about problems with the products it certifies due to mistakes or, more rarely, misconduct. Each alert is based on detailed documentation of the problem in agency files. New York State data on kosher fraud (the only government data available) also suggest that erroneous certification is rare. State records indicate that between 2005 and 2010, the state agency charged with kosher inspection conducted more than 3700 inspections of nearly 900 industrial kosher food production facilities but found only four violations of the state kosher fraud law and issued only sixteen warnings.[75] Although none of this evidence regarding the effectiveness of UL and OU certification is

[74] *Id*. at 97-103.
[75] *Id*. at 106-109. Twenty-two states have kosher fraud laws that prohibit the sale of any food product falsely represented as kosher. Typically, however, state officials charged with enforcement lack any training in Jewish law, and enforcement consists exclusively of responding to complaints. New Jersey and New York are the only states that conduct routine inspection. New Jersey's Bureau of Kosher Enforcement focuses on retail markets and does not routinely inspect industrial production facilities. New York's Kosher Law Enforcement Division employed eleven specially trained kosher inspectors who inspected industrial production facilities throughout the state multiple times each year until 2011, when budget cuts lead the State to dismiss ten inspectors, leaving a Division director without a staff. For further discussion of these and other limitations of state regulation of kosher fraud, see *infra* Part III and *id*. at 112-115.

dispositive, it is sufficient to merit a closer look at how and why private certification works in reducing fire risk and kosher fraud.

II. Key Features of Reliable Private Certification

Private certification is likely to be an effective regulatory instrument only under certain conditions. One set of conditions is related to the structure of the market for certification services, for example, the profitability of certification and brand competition among certifiers. A second set of conditions is related to the social relations among participants in the certification system, for example, a sense of common purpose and a complex network of interpersonal relationships. These two sets of conditions are interrelated: the market for certification services relies on trust and reputation, which are embedded in social relations.[76]

First, *sufficient consumer demand* for certification gives manufacturers incentive to pay for reliable, independent product testing and inspection of their production facilities. Consumers seek the assurances provided by certifiers like UL and the OU, and companies that fail to obtain certification risk losing market share.[77] In the case of fire safety, demand for certification also comes from insurance companies who rely on it to price risk and reduce losses.[78]

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[76] For more detailed analysis of the relationship between market conditions and social context, see Mark Granovetter, *Economic Action and Social Structure: The Problem of Embeddedness*, 91 AM. J. OF SOCIOLOGY 481 (1985); Mark Granovetter, *The Impact of Social Structure on Economic Outcomes*, 19 J. OF ECON. PERSPECTIVES 34-5 (2005).

[77] Leading kosher market analyst Menachem Lubinsky estimates that typically 2 to 20 percent of a product's sales are attributable to kosher certification. He cites the example of Dannon yogurt, whose marketing director claims that, following OU kosher certification in the early 1990s, the company's sales increased $2.2 million in two months. Coors Brewing Company reported that, following kosher certification of its beer, the company's market share increased between 2 and 18 percent in different markets nationwide. Menachem Lubinsky, telephone conversation with the author, September 9, 2011. See also J. M. Regenstein, M. M. Chaudry, and C. E. Regenstein, "The Kosher and Halal Food Laws," 2 *Comprehensive Reviews in Food Science and Food Safety* 113 (2003). For a study on the marketing value of kosher certification, see Michael Kamins and Lawrence Marks, "The Perception of Kosher as a Third- Party Certification Claim in Advertising for Familiar and Unfamiliar Brands," 19 *Journal of the Academy of Marketing Science* 177–185 (1991).

[78] On the importance of profitability to private regulation, see Tim Büthe, *Global Private Politics: A Research Agenda*, 18 BUSINESS AND POLITICS 6, 8 (2010). See also, CHEIT, *supra* note ?, at 180 (discussing the market for

Second, *brand competition among certifiers based on reliability* has led to increasing expertise and accountability. Efforts to build brand value in response to competition led UL and the OU to provide professional training for their personnel and to impose strict ethical codes. Both organizations also instituted new forms of quality control that included multiple layers of oversight, and they improved information management. Brand sensitivity also accounts for their prompt and thorough responses to consumer complaints and their willingness to reveal how they operate through detailed letters to clients, public presentations, print and new media publications, and, in the case of UL, tours of its facilities.[79]

Third, *interdependence among participants in the certification system* gives rise to additional oversight. This is a prominent feature of kosher certification. The value of an agency's certification of a food ingredient—for example, vanilla extract—depends on its acceptability to other agencies certifying products that include the ingredient downstream in the production process—for example, ice cream or cookies. This means that upstream certifiers must meet standards set by downstream certifiers. In turn, downstream certifiers are vulnerable to mistakes by upstream ingredient certifiers, which have the potential to render nonkosher all products made

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safety standards) and David Vogel, *Taming Globalization? Civil Regulation and Corporate Capitalism*, in THE OXFORD HANDBOOK OF BUSINESS AND GOVERNMENT, ed. David Coen, Wyn Grant, and Graham Wilson , 484 (2010) (discussing markets for virtue).

[79] It is worth noting that nonprofit certifiers can be just as brand sensitive and as competitive as for-profit certifiers. Indeed, UL and the OU have used their non-profit status as a key feature of their brand—suggesting that it made them more reliable than for-profit competitors. See KNOWLES, DISASTER EXPERTS, *supra* note ?, at 147-149, 157-160; LYTTON, *supra* note ?, at 48. In 2102, UL created a for-profit testing and certification subsidiary. See John Gallant, *How IT Helped Shape UL's New Business Strategy*, CIO (accessed 6/3/13), http://www.cio.com/article/698876/How_IT_Helped_Shape_UL_s_New_Business_Strategy. On the importance of brand identity among private regulators, see Frederick Mayer and Gary Gereffi , *Regulation and Economic Globalization: Prospects and Limits of Private Governance*, 12 BUSINESS AND POLITICS 9– 11 (2010); Frans van Waarden, *Taste, Traditions, Transactions, and Trust: The Public and Private Regulation of Food*, in WHAT'S THE BEEF? THE CONTESTED GOVERNANCE OF EUROPEAN FOOD SAFETY, Christopher Ansell and David Vogel, eds., 56 (2006). On competition among private third- party certifiers, see MAGNUS BOSTROM AND MIKAEL KLINTMAN, ECO-STANDARDS, PRODUCT LABELLING AND GREEN CONSUMERISM190 (2008), 190. Brand competition requires agencies to be transparent with regard to standards and performance. See Edward Balleisen and Marc Eisner, *The Promise and Pitfalls of Co-Regulation: How Governments Can Draw on Private Governance for Public Purpose*, in NEW PERSPECTIVES ON REGULATION, David Moss and John Cisternino, eds., 135 (2009). On brand competition and food safety standards in Europe, see Thomas Bernauer and Ladina Caduff, *Food Safety and the Structure of the Europe an Food Industry*," in Ansell and Vogel, WHAT'S THE BEEF? 81.

with improperly certified ingredients. Downstream certifiers carefully monitor upstream certifiers to ensure that their standards are acceptable and their inspection routines reliable. Since agencies typically certify different products at different stages of the production process, they operate both upstream and downstream relative to each other, creating a network of interagency oversight. Agencies are also interdependent in the sense that public scandal caused by one agency tends to undermine public confidence in kosher certification more generally, which gives agencies additional incentive to monitor each other and exclude those who fail to meet industry standards.[80]

Interdependence is also a feature of fire safety certification. Insurers' ability to accurately price risk depends upon reliable certification of building materials and consumer products. In turn, the value of certifiers' services to their manufacturing clients depends on insurers' confidence in the certifiers. This interdependence explains insurance companies' representation on UL oversight councils and their major stock holdings in UL. Fire safety certifiers and fire insurers are also hostages to each other insofar as a scandal in either industry reflects poorly on the credibility of the other. A similar sense of collective industry reputation leads many manufacturers' trade associations to require their members to obtain UL certification to assure consumers of the overall safety of whole categories of products.[81]

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[80] LYTTON, *supra* note ?, at 132-3. On supply-chain influence and interdependence generally, see BENJAMIN CASHORE, GRAEME AULD, AND DEANNA NEWSOM, GOVERNING TROUGH MARKETS: FOREST CERTIFICATION AND THE EMERGENCE OF NON- STATE AUTHORITY 23 (2004); NEIL GUNNINGHAM, PETER GRABOSKY, AND DARREN SINCLAIR, SMART REGULATION: DESIGNING ENVIRONMENTAL POLICY 223– 224 (1998); van Waarden, *Taste, Traditions, Transactions, and Trust*, at 56. Tim Büthe and Walter Mattli, *International Standards and Standard-Setting Bodies*, in COEN, GRANT, AND WILSON, OXFORD HANDBOOK OF BUSINESS AND GOVERNMENT, at 442 (discussing interdependence in terms of network externalities). For additional discussions of interdependence and mutual restraint in commercial relations, see MITCHEL ABOLAFIA, MAKING MARKETS: OPPORTUNISM AND RESTRAINT ON WALL STREET, 173 (1996); JOSEPH REES, HOSTAGES OF EACH OTHER: THE TRANSFORMATION OF NUCLEAR SAFETY SINCE THREE MILE ISLAND 2, 44– 45 (1994).

[81] Knowles, *Inventing Safety*, *supra* note ?, at 209-210.

Fourth, *concentration of market power* in the hands of a few large certifiers makes it easier to coordinate the development and enforcement of industry standards. In kosher certification, the Big Five, who control more than 80 percent of the US market, organized the Association of *Kashrus* Organizations (AKO) as a forum for information sharing, deliberation, and standard setting for the industry. While AKO has no formal enforcement powers, it facilitates the communication of reputational information, which is a key source of pressure on agencies to conform to industry standards. In fire safety certification, organizations like the National Fire Protection Association (NFPA) and the American Society for Testing and Materials (ASTM), heavily influenced by market leaders like UL and major fire insurers, play this coordinating function.[82]

Fifth, *a core of active and vigilant consumers* provides additional oversight, gives certifiers quality-control feedback, and puts teeth in reputational sanctions. The 8% of kosher consumers who are religiously observant and eat only kosher food are highly motivated to monitor the reliability of certification. They call agency hotlines to report improperly labeled products—for example, products with a *pareve* label (indicating the absence of any milk products) that list dairy ingredients on the package, packages with agency symbols that appear to be counterfeit, or items that contain ingredients that they suspect are not kosher. Many of these consumers closely monitor agency publications for consumer alerts concerning improperly labeled products or unreliable certifications, and they disseminate this information through social networks. Since certification agencies' brand value depends upon their reputation among these vigilant consumers, agencies have a strong incentive to avoid mistakes and misconduct, and to report

[82] On concentration in private regulation, see Tetty Havinga, *Private Regulation of Food Safety by Supermarkets*, 28 LAW & POLICY 528 (2006). Of course, concentration of market power carries risk of anticompetitive collusion. On antitrust concerns in kosher certification, see LYTTON, *supra* note ?, at 161-163 and in fire safety certification, see KNOWLES, DISASTER EXPERTS, *supra* note ?, at 159-160.

them promptly when they occur.[83] In fire safety certification, insurers provide a similar vigilance. They investigate fires for signs that products were improperly certified or that certification standards are too low, and they communicate the results to certifiers and disseminate them through trade associations.[84]

The examples of fire safety and kosher food illustrate how these market conditions are embedded in social relations that support reliable private certification. In each case, certification agency personnel are motivated by an *industrial morality*—a shared sense of mission that counteracts incentives to cut corners and promotes cooperation between competing certifiers.[85] Kosher certification is not just a business. For the rabbis who staff certification agencies, it is also a sacred trust. The same is true of fire safety engineers—"anti-combustion missionaries"—whose efforts were typical of progressive-era initiatives that combined rational policy analysis with evangelical passion for social reform.[86]

In addition to industrial morality, *social networks* provide the medium for trust and reputation that supports reliable private certification. At AKO meetings, participants from different kosher certification agencies socialize and pray together. The rabbis who manage these agencies also frequently hold positions of authority in their local Jewish communities, many as congregational rabbis or respected teachers, interacting closely with community members, who

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[83] On the role of kosher consumers, see Shayna Sigman, *Kosher without Law: The Role of Nonlegal Sanctions in Overcoming Fraud within the Kosher Food Industry*, 31 FLORIDA STATE UNIVERSITY LAW REVIEW 584 (2004); Shana Starobin and Erika Weinthal, *The Search for Credible Information in Social and Environmental Global Governance: The Kosher Label*, 12 BUSINESS AND POLITICS 21– 22 (2010). On active consumers and other civil-society groups in private regulation more generally, see Büthe, *Global Private Politics*, at 12; Mayer and Gereffi , *Private Governance*, at 11– 13; Unni Kjaernes, Arne Dulsrud, and Christian Poppe, *Contestation over Food Safety: The Significance of Consumer Trust*, in ANSELL AND VOGEL, WHAT'S THE BEEF? 62. For a suggestion that consumer markets may be efficient even if only a small proportion of consumers are sophisticated in their purchasing choices, see Alan Schwartz, *How Much Irrationality Does the Market Permit?*, 37 J. OF L. STUD. 131, 131-137 (2008). For a striking example of consumer vigilance in the kosher food industry, see LYTTON, *supra* note ?, at 117.

[84] CHEIT, *supra* note ?, at 180-184.

[85] On industrial morality, see, Neil Gunningham and Joseph Rees, *Industry Self- Regulation: An Institutional Perspective*, 19 LAW AND POLICY 376-380 (1997).

[86] LYTTON, *supra* note ?, at 134-135; KNOWLES, DISASTER EXPERTS, *supra* note ?, at126.

are also kosher consumers. Agency personnel form personal bonds with their food-industry clients, many of whom they have been working with for decades. Personal ties also exist among religiously observant kosher consumers, ranging from close connections between congregants to more extended Internet exchanges carried on through postings on kosher-food websites.[87]

These various relationships constitute a complex network that enhances the regulatory performance of the kosher certification system in a number of ways. The extent to which rabbinic administrators and managers all know each other increases social pressure to conform to industry standards. Network theory refers to this as "network density" and defines it as the proportion of links between individuals to the total number of possible links within the network. High network density among rabbinic administrators and managers constitutes a "small world" that strengthens industrial morality and increases social cohesion within the group. In addition, extensive interpersonal links within and between agency, food-company, and consumer networks facilitate the diffusion of consumer alerts and reputational information.[88]

In fire safety, certifiers, insurers, manufacturers, and government officials communicate frequently on an ongoing basis when serving on committees and attending meetings sponsored by UL and various membership organizations, such as the NFPA and ASTM. While the fire safety community is less intense and more diffuse than the tight-knit Orthodox Jewish community, it nevertheless enhances regulatory performance in the same ways.[89]

To summarize, the effectiveness of UL and the OU allow one to identify conditions that support reliable private certification. In both cases, the structure of the market for certification

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[87] On social networks and reputational sanctions, see Lisa Bernstein, *Opting Out of the Legal System: Extralegal Contractual Relations in the Diamond Industry*, 21 J. Leg. Stud. 115 (1992); Barak Richman, *How Community Institutions Create Economic Advantage: Jewish Diamond Merchants in New York*, 31 Law & Social Inquiry 383 (2006); Sigman, *supra* note ?; Starobin and Weisenthal, *supra* note ?.

[88] On complex social networks, see Michael Ferrary and Mark Granovetter, *The Role of Venture Capital Firms in Silicon Valley's Complex Innovation Network*, 38 ECONOMY & SOCIETY 332 (2009). On network density, see Granovetter, *Impact of Social Structure*, *supra* note ?, at 34-5 (2005); LYTTON, *supra* note ?, at 134-5.

[89] KNOWLES, DISASTER EXPERTS, *supra* note ?, at 129-140.

services creates economic incentives for certifiers and their industry clients to maintain standards that satisfy consumers and others who rely on their certification, such as insurers. A strong industrial morality among certifiers provides social norms that reinforce these economic incentives, and a complex social network puts social pressure on certifiers to adhere to these norms and disseminates reputational information about certifiers and manufacturers. Of course, these conditions do not always exist, or they may be underdeveloped, in which case private certification may not perform as well as the two examples presented here.

III. The Comparative Institutional Advantages of Private Certification

In their formative decades, both UL and the OU offered an alternative to government regulation. Government efforts to reduce fire risk and kosher fraud were frustrated by political opposition, lack of expertise, and insufficient resources. Today, the situation is different. In fire safety, private certification is intertwined with government regulation in a complex public-private mix of consensus standards and government mandates, a system in which private certifiers and government agencies frequently rely upon and complement each other.[90] In kosher certification, private certification and government regulation work side-by-side. Private kosher agencies' informal sanctions are ultimately backed by government prosecution and/or recourse to the civil courts to deal with the most egregious cases of fraud.[91]

The severe limitations on government regulation of fire safety and kosher food during the formative years of UL and the OU highlight the comparative institutional advantages of private

[90] *Id.* For a brief history of the consensus standard system in fire safety, see *History of the NFPA Codes and Standards-Making System*, NATIONAL FIRE PROTECTION ASSOCIATION (accessed 6/3/13), http://www.nfpa.org/assets/files/PDF/HistoryNFPACodesStandards.pdf. For an example of incorporation of consensus standards in government fire safety regulation, see *Fire Safety*, OCCUPATIONAL SAFETY & HEALTH ADMINISTRATION (accessed 6/3/13), http://www.osha.gov/SLTC/firesafety/. For an overview of local code authority reliance on UL, see *Code Authorities*, UL (accessed 6/3/13), http://www.ul.com/global/eng/pages/offerings/perspectives/regulator/.

[91] LYTTON, *supra* note ?, at 120-121.

certification over government regulation. The continued profitability and reliability of UL and the OU up to the present suggests that these comparative advantages may persist even when private certification coexists with government regulation. Thus, government regulation need not displace private certification. Moreover, insofar as the two are complementary, the comparative advantages of private certification are not an argument against government regulation.

Before examining the comparative institutional advantages of private certification over government regulation, a few caveats are in order. First, no system of regulation is immune from mistakes and misconduct. Like all regulatory instruments and institutions, private certification is imperfect. Consequently, when discussing the comparative institutional advantages of private certification over government regulation, the comparison will be between admittedly imperfect regulatory alternatives.[92] Moreover, the comparative institutional advantages of private certification, which are so pronounced in the fire safety and kosher food examples, depend upon the presence of the market conditions and social relations identified in Part II. In addition, these comparative advantages will vary from case to case, depending on the private certifier and the government agency to which it is being compared. Finally, not all of the advantages discussed below apply equally to all private certification systems.

One advantage of private certification over government regulation is *greater technical expertise*. Government regulators frequently rely on private product-safety standards to give their own regulations more credibility. Sometimes government regulations modify a private standard; often, they simply incorporate it by reference.[93] Private certifiers typically have superior "working knowledge of technical terms and basic engineering considerations" with regard to

[92] NEIL KOMESAR, IMPERFECT ALTERNATIVES: CHOOSING INSTITUTIONS IN LAW, ECONOMICS, AND PUBLIC POLICY 3 (1994); PETER H. SCHUCK, THE LIMITS OF LAW: ESSAYS ON DEMOCRATIC GOVERNANCE 424 (2000).
[93] CHEIT, SETTING SAFETY STANDARDS, at 225. See also Peter L. Strauss, *Private Law Organizations and Public Law*, http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2194210 (accessed 4/29/29).

particular products, "and they understand the practical implications of commercial use" better than their government counterparts, according to Cheit.[94] In kosher certification, government regulators have less expertise than private certifiers in determining how the traditional laws of kosher observance apply to modern industrial food production. Kosher certification agencies are advised by leading rabbinic experts in Jewish law and run by managers with extensive training in Jewish law coupled with practical experience in food chemistry, food technology, marketing, information technology, and commercial law. By contrast, most state officials charged with enforcing kosher fraud laws have little or no training in Jewish law.[95]

Private certification frequently provides *better inspection and monitoring coverage of regulated entities*. For government regulators, inspection and monitoring strain agency budgets. By contrast, for private certifiers, inspection and monitoring generate fees. The income received from inspection services prompts UL to inspect facilities at least four times per year—"an approach that far exceeds any public enforcement scheme."[96] Similarly, kosher certification agencies have strong financial incentives to expand their inspection and monitoring activities, while government kosher inspection in the only two states that provide it—New York and New Jersey—has been drastically curtailed in the past few years due to budget cuts.[97] Aside from incentives, private certifiers also face fewer obstacles to monitoring and enforcement. They are

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[94] However, according to Cheit, government regulators typically are better than private certifiers at obtaining information about real-world experience with products and may be just as competent as private certifiers in conducting applied research that informs standard setting. See CHEIT, *supra* note ?, at 196-202.

[95] LYTTON, *supra* note ?, at 116. On expertise in private regulation, see Edward Balleisen, *The Prospects for Effective Coregulation in the United States: A Historian's View from the Early Twenty- First Century*, in GOVERNMENT AND MARKETS: TOWARD A NEW THEORY OF REGULATION, Edward Balleisen and David Moss, eds., 454 (2010); CHEIT, *supra* note ?, at 14– 15, 196– 202; GUNNINGHAM, GRABOSKY, AND SINCLAIR, SMART REGULATION, at 200. On information deficiencies and expertise deficits in government policymaking, see PETER H. SCHUCK, WHY GOVERNMENT FAILS SO OFTEN AND HOW IT MIGHT DO (A LITTLE) BETTER (forthcoming 2014) ch. 6.

[96] CHEIT, *supra* note ?, at 183. This figure is from the late 1980s. The UL website states that the organization conducts routine unannounced inspections "on a periodic basis" of manufacturing facilities that produce items that it certifies. *Follow-Up Services FAQ*, http://www.ul.com/global/eng/pages/corporate/contactus/faq/general/fus/ (accessed 7/25/13).

[97] LYTTON, *supra* note ?, at 117.

not limited by local, state, or national jurisdictional boundaries, which makes it possible for them to more easily provide on-site inspection nationally and around the world.[98]

Government agencies could, theoretically, charge fees for inspection and monitoring. Indeed, government routinely charges fees for services such as permitting and licensing, but proposals to charge regulated entities fees for inspection and monitoring typically face stiff political resistance.[99] Moreover, government fees are designed merely to cover costs, not increase profits, so they do not offer the same level of incentive as private fees to expand inspection and monitoring.

Private certification is often *more proactive and prospective* than government regulation. Private product certifiers "intervene relatively early in the life cycle of an issue, often in anticipation of problems rather than in response to them," whereas government regulation is generally more reactive to specific incidents.[100] Similarly, private kosher certifiers actively seek out problems before they affect consumers and set new policies to avoid trouble later. They are more likely to act as soon as a problem arises and to be involved in an ongoing basis to correct it. By contrast, state officials are merely reactive to complaints about kosher fraud, and they typically wait to intervene until a major scandal attracts widespread public attention.[101]

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[98] On the monitoring and coverage of private regulators, see Balleisen, *supra* note ?, at 455; GUNNINGHAM, GRABOSKY, AND SINCLAIR, *supra* note ?, 200. On the transcendence of national boundaries by private regulators, see Balleisen, *supra* note ?, at 464; Tim Büthe, *Private Regulation in the Global Economy: A (P)Review*, 12 BUSINESS & POLITICS 4 (2010). On trans jurisdictional limitations of government regulation, see SCHUCK, WHY GOVERNMENT FAILS, *supra* note ?, ch. 7.

[99] See, e.g., Helena Bottemiller, *Hamburg: FDA Needs More Resources for Food Safety*, FOOD SAFETY NEWS, March 1, 2012, (accessed 4/29/13) http://www.foodsafetynews.com/2012/03/commissioner-hamburg-fda-needs-more-resources-for-food-safety/. For an example of government fees designed to defray the costs of permitting and licensing, see *Prescription Drug User Fee Act (PDUFA)*, U.S. FOOD AND DRUG ADMINISTRATION (accessed 6/3/13), http://www.fda.gov/ForIndustry/UserFees/PrescriptionDrugUserFee/default.htm.

[100] CHEIT, *supra* note ?, at 202-3.

[101] LYTTON, *supra* note ?, at 117-8. On the proactiveness of private regulators, see Timothy Sinclair, *Credit Rating Agencies*, in COEN,WYN, AND GRAHAM, OXFORD HANDBOOK OF BUSINESS AND GOVERNMENT, at 424; Balleisen, *Effective Coregulation*, at 454; CHEIT, SETTING SAFETY STANDARDS 202– 204; Lawrence Busch, *Quasi- States? The Unexpected Rise of Private Food Law*, in VAN DER MEULEN, PRIVATE FOOD LAW 63.

Private certification can be *more responsive* to both regulated industries and consumers. The effort required to pass legislation or promulgate regulations often means that if government regulators do manage to establish product-safety standards, they are very unlikely to revise them in light of industry or consumer reaction. Federal agencies like the Consumer Products Safety Commission and the Occupational Safety and Health Administration typically attend to fire safety hazards only following a crisis with a one-shot intervention that is seldom revisited or revised. "As a result," explains Cheit, "public standards are often confined in scope, and they tend to stay fixed in their original form." By contrast, private standard setting agencies and testing labs routinely review and, if necessary, revise their standards in light of experience.[102]

In kosher food regulation, state legislators and state agency officials—for whom adulteration and mislabeling of kosher food is a relatively low priority—are not likely to vigorously pursue consumer complaints, especially in states where religiously observant Jews are a small minority with little electoral influence. Moreover, legislative and administrative rule-making processes are very slow, frequently taking years to produce results. By contrast, kosher certification agencies owe the brand value of their services to their reputation among consumers, and they are motivated by a sense of religious mission. They solicit consumer feedback and respond to concerns through their public presentations, telephone hotlines, websites, newsletters, and magazines. Furthermore, kosher certification agencies can respond to consumer concerns more

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[102] CHEIT, *supra* note ?, at 204. On responsiveness and accountability in private regulation, see Tim Büthe, *Global Private Politics*, at 18; Fuchs, Kalfagianni, and Havinga, *Actors in Private Food Governance*; Daniel Esty, *Good Governance and the Supranational Scale: Globalizing Administrative Law*, 115 YALE LAW JOURNAL 1490 (2005); J. J. BODDWYN, ADVERTISING SELF- REGULATION AND OUTSIDE PARTICIPATION 11 (1988), 11; CHEIT, *supra* note ?, 203-204, 206, 212–218; Yilmaz, *Private Regulation*. For an overview of critiques suggesting that government regulation often lacks accountability, see JERRY MASHAW, RICHARD MERRILL, AND PETER SHANE, ADMINISTRATIVE LAW: THE AMERICAN PUBLIC LAW SYSTEM, 6th ed., 34– 45, 49– 56 (2009). On rigidity in government policymaking, see SCHUCK, WHY GOVERNMENT FAILS, *supra* note ?, ch. 6. For a suggestion that responsiveness to public petitions interfered with proper priority setting at the CPSA, see Teresa M. Schwartz, *The Consumer Product Safety Commission: A Flawed Product of the Consumer Decade*, 51 GEO. WASH. L. REV. 32 (1982)

quickly by instituting kosher policy changes without the procedural hurdles faced by government regulators.

Regulation by private certification *facilitates cooperation* by regulated entities. Within ongoing private agency-client relationships, manufacturers are eager to satisfy the demands of certifiers upon whom they rely for the marketability of their products. Companies come to see private agencies as marketing partners rather than police. Electrical equipment and consumer product manufacturers need UL or some equivalent certification in order to compete in the market for their products, and food companies rely on kosher certifiers for access to the kosher market.[103]

Private certification is often *more efficient* than government regulation. Competition among certifiers provides incentives for them to cut costs in order to keep their fees as low as possible while at the same time maintaining high standards in order to protect their brand value. By relying primarily on informal sanctions—such as the refusal to certify—private certifiers do not incur the costs associated with passing legislation, making administrative rules, filing enforcement actions, establishing guilt in legal proceedings, and defending appeals. Moreover, as already mentioned, private certifiers often have a more cooperative relationship with the companies that they regulate. In addition, since private certifiers are motivated to regulate in part by industry demand, they are less likely than government regulators to develop standards whose costs outweigh their benefits. There is, of course, no demand for such standards among regulated industries.[104]

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[103] On cooperation in private regulation, see Balleisen, *supra* note ?, at 458-459. For extensive discussion of the adversarial nature of government regulation, see EUGENE BARDACH & ROBERT KAGAN, GOING BY THE BOOK: THE PROBLEM OF REGULATORY UNREASONABLENESS (2d ed. 2002); ROBERT KAGAN, ADVERSARIAL LEGALISM: THE AMERICAN WAY OF LAW (2001).

[104] On the lower standard-setting and enforcement costs of private regulation, see BODDWYN, *supra* note ?, at 8; CHEIT, *supra* note ?, at 194– 195; Barak Richman, *How Community Institutions Create Economic Advantage: Jewish Diamond Merchants in New York*, 31 Law & Social Inquiry 384 (2006); Sigman, *supra* note ?, at 560;

IV. Concerns about the Legitimacy of Private Certification

Some critics question the legitimacy of private regulation. They assert that it does not allow sufficient participation among stakeholders, that it lacks transparency, and that private certifiers are not democratically accountable in the way that government regulators are. For example, in one study, Doris Fuchs, Agni Kalfagianni, and Tetty Havinga evaluated the democratic legitimacy of private standard setting in the retail food industry aimed at promoting consumer protection, fair labor practices, and sustainable farming. They found that "decision-making bodies frequently do not allow participation by all groups affected by these standards" and that resource disparities "prevent equal participation." Moreover, they observed that many standard-setting bodies are not open about their processes and publish limited information about the issues they address. Finally, they discerned a lack of accountability in terms of external audits and performance reviews available to consumers and the general public. "[I]t should not come as a surprise," they concluded, "that most private food standards primarily reflect the interest of retailers in minimizing the risk of scandals and marketing their products. . . . The result of our analysis of the democratic legitimacy of private retail food governance, then, is not an optimistic one."[105]

Starobin and Weisenthal, *supra* note ?, at 28.On cost-benefit analysis in private standard setting, see CHEIT, *supra* note ?, at 117-118, 180-181; Yilmaz, *supra* note ?.

[105] Fuchs, Kalfagianni, and Havinga, *Actors in Private Food Governance*, at 1, 10–12; For additional discussion of the legitimacy of private regulation, see BOSTROM AND KLINTMAN, ECO- STANDARDS, 76– 82; EVA SØRENSEN AND JACOB TORFING, EDS., THEORIES OF DEMOCRATIC NETWORK GOVERNANCE (2007), chps. 8, 14, 15, 16; Busch, *Quasi- states*, at 64– 66; Lisa Sharma, Stephen Teret, and Kelly Brownell, *The Food Industry and Self- Regulation: Standards to Promote Success and to Avoid Public Health Failures*, 100 AMERICAN JOURNAL OF PUBLIC HEALTH 240 (2010).

A fair evaluation of any regulatory instrument, however, requires recognition that it is always one among a number of imperfect alternatives.[106] Government regulation often falls short of ideals of participation, transparency, and accountability. For example, notice-and-comment rulemaking by government agencies can be heavily influenced behind the scenes by industry stakeholders. A recent study by Wendy Wagner, Katherine Barnes, and Lisa Peters examined rulemaking by the U.S. Environmental Protection Agency involving standards for the release of air toxins from major sources. They found that, prior to publication of proposed rules for public comment, agency contacts with affected parties were "extensive" and were "dominated by regulated parties." During the notice-and-comment period, formal comments came "predominantly from regulated industry," and changes to the proposed rules reflected this imbalance and generally favored industry. After rules were promulgated as final, regulated parties frequently brought legal challenges and obtained additional revisions in nonpublic settlement negotiations. [107]

The examples of private certification by UL and the OU compare favorably in terms of participation, transparency, and accountability with notice-and-comment rulemaking as described by Wagner et al. UL's procedures allow anyone to suggest a new standard or revision of an existing one. UL assembles Standards Technical Panels, composed of manufacturers, technical experts, government officials, consumers, and others "materially affected," to review suggestions and develop them into specific standards. These panels then solicit and respond to public comments. Finally, the panels either adopt proposed standards by consensus or revise

[106] On comparative institutional analysis, see KOMESAR, IMPERFECT ALTERNATIVES, at 3; SCHUCK, LIMITS OF LAW, at 424.
[107] Wendy Wagner, Katherine Barnes, and Lisa Peters, *Rulemaking in the Shade: An Empirical Study of EPA's Air Toxic Regulations*, 63 ADMINISTRATIVE LAW REVIEW 119 (2011).

them for further consideration.[108] UL publicizes its standard-setting activities and lists the products it certifies. This type of transparency has, from the outset, been central to UL's strategy of building its reputation for reliability and, consequently, its brand value.[109]

Admittedly, the OU and other kosher agencies do not allow the same level of stakeholder participation in standard setting as UL, but agency magazines, books, websites, hotlines, and social networks promote considerable transparency aimed at informing food companies and kosher consumers. Agencies explain in great detail the reasoning behind their standards in a steady flow of articles published in magazines and posted on websites. For example, the OU has published a series of books detailing its certification standards and policies in the oil, baking, fish, and produce industries. Agency hotlines field questions about standards and policies, and agency personnel regularly make presentations, conduct panel discussions, and hold question-and-answer sessions at trade association conferences and in Jewish communities around the country.[110] Private certifiers may be more accountable than government to consumers and regulated entities. As already mentioned in Part III, government is typically slower to respond to calls for new standards and less likely to revise existing ones than UL or the OU.

Of course, participation, transparency, and accountability vary widely among different examples of government regulation and private certification. I have, admittedly, offered only summary statements of the findings from two studies and generalities about UL and the OU. Nevertheless, this evidence does suggest that assumptions about the inferior legitimacy of private regulatory instruments as compared to government regulation ought to be set aside in favor of more detailed case-by-case analysis.

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[108] Interest Categories, (accessed 4/29/13) http://www.ul.com/global/eng/pages/solutions/standards/developstandards/participation/membershipcriteria/ (accessed 4/29/13); Flow Chart, http://csds.ul.com/Tutorial/stp_flow_chart.pdf.
[109] KNOWLES, DISASTER EXPERTS, *supra* note ?, at 149.
[110] LYTTON, *supra* note ?, at137-8.

V. Conclusion

UL and the OU offer examples of how private certification can overcome political and resource constraints that frustrate government regulation. The conditions that favor reliable private certification include structural features of the market for certification services—sufficient consumer demand, brand competition, interdependence, concentration of market power, and consumer vigilance—within a social context of an industrial morality that creates peer pressure to maintain high standards and a complex social network that conveys reputational information. Reliable private certification frequently has a number of comparative institutional advantages over government regulation in terms of technical expertise, flexibility, monitoring, responsiveness, cooperation, and efficiency. The legitimacy of private certification rests on stakeholder participation, transparency, and accountability.

The reliability and the legitimacy of UL and the OU are connected. In both cases, competitive markets for certification make certifiers highly brand sensitive, and this translates into a desire to build and maintain a good reputation among industry clients, consumers, and others who rely on certification. These reputational concerns have led both UL and the OU to improve the reliability of their certification services and to inspire confidence in them through stakeholder participation, transparency, and accountability.

These two examples of reliable private certification offer an interesting contrast with government regulation by administrative agencies. It is commonly argued that effective agency regulation requires political and legal accountability in the form of legislative oversight and judicial review, as well as insulation from the influence of private interests, especially those that

involve personal ties or offer potential financial rewards to regulators.[111] In the context of government agency regulation, independence from legislative and executive oversight, absence of judicial review, close ties to regulated entities, and a fee-for-service organizational model are a recipe for agency capture and regulatory failure.[112]

By contrast, in the context of private certification, these same attributes are the ingredients of success. UL and the OU are successful because they are free of the political accountability and legal constraints that have hampered government regulation of fire safety and kosher food. Moreover, the reliability of UL and OU certification is fueled by market incentives and reinforced by social relationships. Here, successful private regulation converts market incentives and social influences from regulatory vices into virtues.

[111] See, e.g., JERRY L. MASHAW, RICHARD A. MERRILL, AND PETER M. SHANE, ADMINISTRATIVE LAW: THE AMERICAN PUBLIC LAW SYSTEM, 6th ed. (2009).
[112] *Id.* at 49-56. See also, DANIEL CARPENTER AND DAVID A. MOSS, PREVENTING REGULATORY CAPTURE: SPECIAL INTEREST INFLUENCE AND HOW TO LIMIT IT (2014).