Cynthia Day Wallace

Legal Control of the Multinational Enterprise

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LEGAL CONTROL OF THE MULTINATIONAL ENTERPRISE

National Regulatory Techniques
and the
Prospects for International Controls

Cynthia Day Wallace

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To I.H.S. and B.L.H.,
both of whom sustained
me in their respective spheres.

FOREWORD

Although the cascade of publications about multinationals quickens constantly, Dr. Wallace's book has virtues that recommend it to even the busiest reader. Above all, it is free of the awed preconceptions that permeated so much of the early writings on the topic — the *Sovereignty at Bay, Le Défi américain, Global Reach, Invisible Empires* generation of analysis. Since the early 1970's enough has been written to justify the 426 page bibliography patiently assembled by the United Nations Centre on Transnational Corporations. The author is obviously fully aware of that flood, including the very substantial part of it that is only accessible in French and German, but does not leave us to drown in it. Her presentation is compact, though comprehensive, and her style is crisp and lucid.

The unblurred focus of this book is made possible by the decision to concentrate on relations between multinationals and the states of the developed world. Since so much of the writing has been from the perspective of the Third World (even when the author is thoroughly American or European) this comes at first as a shock. Upon reflection one sees that not only is this an entirely workable division of labor but that it encompasses the part of the situation which has by far the greatest potential significance for us. The future of the multinational, even if one includes the mineral extracting enterprises, lies not with the less developed world but within the industrialized capitalist states. The statistics on the quantity of foreign direct investment, its sources and its destinations, clearly show that this is the important stage to watch.

The drama that will be played out on it over the next few years will be a gripping one. The logic of the multinationals, a logic which has been worked out in the course of their rapid recent growth, hinges upon their having free access to diverse markets and resources so that they can combine factors found in different states to make profit for themselves and benefits for those around them. States are always tempted to try to tilt the balance so that they may have more of the benefits for their own, a temptation that was resisted collectively with fair success in the first two post war decades but which is assuming a new attractiveness for governments faced with capital flight, balance of payments weakness and unemployment. The recent tensions between the United States and Canada over the latter's National Energy Policy and the worries in other states about the tendency of the Mitterand government in France to go its own way are seen by some observers as symptoms of a new trend towards autarchy.

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In a world where nations let their economic policies drift apart it goes hard for multinationals. Dr. Wallace describes in useful detail some of the past episodes in which national policies have put pressure, subtle or otherwise, upon foreign investors. While they spread out over time from the Fruehauf episode (p.100) to the British government's pressure for renegotiating the deal as to North Sea oil rights (p.238), one does have a sense that the pace may be picking up. Faced with such pressures, the resistive capacity of the multinational proves not to be anywhere near as formidable as once imagined. Its political power in the host state where it is a stranger, and a rich one to boot, is not great. Its economic leverage may have been weakened by the worldwide recession; the time when the president of Ford Motor Company could threaten Great Britain with a transfer of its attentions to another country unless its working conditions were improved seems long ago. The home state is not apt to be willing to incur great risks in order to protect one of its corporate citizens, especially when it has been brought home to viewers that outbound foreign investment may have harmful effects upon the state it is leaving.

All of this centrifugal tendency comes about during times when the basic economic laws of international cooperation hold just as true as ever before. Each gesture of economic nationalism has its costs. If Canada in fact retakes much of its energy business from American oil companies that will draw down on the domestic supply of capital. In the second line, it will discourage other investors from selecting Canada. In the third, it may cause United States moves to hamper Canadian firm's activities south of the border. As multinational firms have caused the originally unilateral outpouring of investment from the United States to be matched by capital flows toward the United States the connections are complex enough that they should give states pause at the thought of hacking away at the structure. It remains to be seen how far governments will, nonetheless, go to safeguard their own short-range national economic interests and their general interest in independence and autonomy. For a perspective from which to view both the national initiatives and the attempts to build and preserve international restraints on such moves we cannot do better than to turn to this magisterial work.

Detlev F. Vagts

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In addition I should like to acknowledge the contribution made by conversations with and/or written comments from the following persons, each of whom read a selected chapter of the work: Prof. Detlev Vagts of Harvard Law School, who also very kindly agreed to write the Foreword; Prof. Oscar Schachter of Columbia University Law School; Frederick M. Rowe, Visiting Lecturer at Yale Law School and past Chairman, Section of Antitrust Law, American Bar Association; Prof. Dr. Karl Doehring of the University of Heidelberg Faculty of Law and co-Director of the Max Planck Institute of Comparative Public Law and International Law, Heidelberg; and Prof. Dr. Ernst-Joachim Mestmäcker, co-Director of the Max Planck Institute of Private International Law, Hamburg; also Professor D.J. Harris of Nottingham University, England, who read the work in its entirety and kindly noted down his useful comments.

Meriting a medal for her intelligent decoding of my manuscript, replete with colour-coded signs and symbols, arrows and insertions, is Rachel Baird, who faithfully typed many hundreds of pages of manuscript, and even saw to it that I sometimes ate, and to her family who participated indirectly by their patience and sacrifices. For typing of many pages of revisions, Margot Lintaller's cheerful willingness and competence was also deeply appreciated, as was that of

law students Lisa Granik and Janet Levy for their dedicated assistance during the proofing and indexing phase.

Despite the many persons who lent their wisdom and skills to my efforts, the full and sole responsibility for the content here presented, including any errors of fact, judgment or analysis, remain my own.

Cynthia Day Wallace
Heidelberg
March 1981

INTRODUCTION

The aim of the present work is to determine the desirability of international controls over multinational business activity. In order to determine the desirability of such controls - proceeding on the initial assuption that multinational enterprises (MNEs) do need some kind of control - we must confront the issue of whether the MNE is at present subject to any form of control, or whether, as is popularly alleged, it runs rough-shod, unfettered and uncontrolled across national boundaries, with no heed to national jurisdictions and no answerability to higher authority. If substantial controls do exist, what aspects of MNE activity do they cover, and are they adequate to control all aspects of such activity that are deemed to need regulating? If they are inadequate, in what areas are they inadequate, and could any such control-deficient areas conceivably be covered satisfactorily by international control measures?

Due to the fact that the largest percentage of MNE activity is currently taking place in the industrialized nations, and that it is consequently in these nations that the most innovative legislation is to be found relating to multinationals, and for other reasons elaborated in the text, it is the highly industrialized economies which will be the focus of the present work, with particular reference to the U.S.A., Canada, Great Britain, France, Germany and Japan. It is hoped that the focus on the industrialized world will not deter those interested in the developing nations from reading the following pages. Although many of the problems of these two economic sectors differ sufficiently to require separate treatment in most respects, the material herein is relevant for all those concerned with regulatory measures surrounding the multinational enterprise, whether in the developed or the developing world, considering that national legislation reasonably accurately reflects the problem areas, and that any truly international controls will, by definition, affect all economic sectors.

While concentrating on the six highly capital-intensive states selected to illustrate the current trends in MNE regulation, the emphasis in the present study is not one of comparative law, but centers rather upon the major legal *techniques* of control, drawing practical examples from the relevant legislation and case law of those industrialized states most active in both inward and outward foreign direct investment, as enumerated above.

The fact that there is no allusion to the 'problem of control' is not accidental. This work addresses itself to the 'issue of control'. Whether or not control is, in

fact, a 'Problem' is a debatable and a highly subjective question. It would seem safe to assume, considering the spate of literature in socio-economic and political as well as, more recently, in legal circles, to say nothing of the intense international activity centering around the subject in such bodies as the UN, OECD, ILO, UNCTAD, ICC and other international organizations, that *a* problem exists. Whether or not the problem is one of control of multinationals *per se* is in this writer's opinion a moot point, for which this study may provide some possible insights.

It is this writer's opinion that control of the multinationals, as such, (1) is not really, or (2) has ceased to be, a serious 'Problem'. This in not meant to be expanded to imply that control has ceased to be an *issue*, and an issue, indeed, within which very real problems do arise. The statement is nonetheless a bold one, and requires clarification.

First, one can say that the control of the multinational *per se* (1) is not really a 'Problem', in the sense that the accusations of abuses and excesses often directed at the MNEs - and in some cases substantiated - are also perpetrated by purely national corporate 'giants', to say nothing of other, non-corporate organized groups. This is in no way to excuse the abuses, but merely to point out that the 'Problem' may not be exclusively that of controlling the MNE, as such enterprises are not the sole perpetrators of questionable business practices. In fact, statistics show that in comparison with their national counterparts, MNEs have, on the whole, a better record of service to the community than do national firms. This is no doubt partially due to concessions sometimes exacted by a host state in return for the 'privilege' of direct investment extended to the foreign firm - i.e., certain services to the local community being made conditions of entry by the host government - and partially from the realization on the part of the foreign enterprise itself that it will be under closer scrutiny, as a 'foreigner', and viewed with more suspicion than a domestic firm and that consequently, if it does not make a significant contribution to the community, or at least conduct itself according to the 'rules' of 'good corporate citizenship', it may be asked to leave.

It is obvious, however, that a foreign presence does have some implications which are inapplicable when it comes to domestic enterprises, and this fact will not be overlooked in the present study. It is equally obvious that certain control measures will be primarily directed at those business enterprises whose own control centers are located outside the jurisdiction of the host. It thus becomes clear that it is less the abuses themselves than it is the abuses being committed by a foreign element which has become the issue. The question still remains, however, as to whether the issue, or 'Problem', is one of controlling the MNE *per se*. To this we must respond that even when concentrating on 'foreignness',

multinational enterprises are only one vehicle for foreign direct investment. Such investments are also made by individuals, by banks, by insurance companies, by partnerships and by other types of business enterprises which are equally capable of holding a controlling interest in the host concern and influencing internal economics as are the multinationals themselves. The present writer would therefore submit that the real issue in this area is not one of control of the multinational enterprise, but one of control of any form of foreign direct investment involving share ownership to a percentage deemed by the individual host state to carry with it undue foreign control over important sectors of its economy.

The multinational has become the scapegoat for all ills resulting from foreign commercial presence in any form. Yet when examining control legislation, it is virtually impossible to single out the MNE as a distinct target. Very little legislation refers to multinationals as such; the laws tend to be aimed at foreign direct investment in general. From the case law, on the other hand, illustrations can be extracted which deal directly with problems arising out of identifiable MNE activity. Where appropriate, then, throughout the body of the work, 'case law' has been drawn upon in an attempt to separate out the MNE from other forms of foreign direct investment, in this limited area, at least. It is in the case law, and in the legislative framework supporting it, that we can find evidence to support the proposition that, although problems inevitably arise out of MNE activity, as out of all brands of commercial activity, the control of the MNE *per se*, while an 'Issue', is in fact not a 'Problem'. In other words, the individual problems which arise within the larger Issue can be dealt with, for the most part, within the existing legal framework, particularly in the Western systems. (This subject, and an attempt at identifying some of those areas which cannot be adequately dealt with within the existing legal framework, is expanded in the text.) As one writer has expressed it: "There are always potential, sometimes even endemic, disputes between the foreign firm and its hosts, but these do not usually become critical, at least in the industrialized countries."[1] And, in the words of another writer, in the case that

> ...the conflict between the international economy and a given national economy or between the aims and goals of a multinational corporation and a given national economy is not reconcilable, then that economy is not suited to the operations of a multinational corporation, and the latter should go elsewhere in the world for its investments.[2]

1. Brooke and Remmers, eds. *The Strategy of Multinational Enterprise: Organization and Finance* (London: Longmans (1970)), at 614.

2. Rogers, "Multinational Corporations: A European View", in Blake, ed., *The Annals of the*

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Secondly, one can say that the control of the multinational (2) has *ceased* to be a problem because "[e]vidence exists in the actions of both the international companies and host governments that the role of foreign direct investment may be diminishing on the international scene..."[3] or, as it has been picturesquely described, the shadow of the multinational enterprise is caused by the setting rather than the rising sun.

One substantial addition may be necessary here; it might be more realistic to say that the shadow cast by the *American* multinational comes from the setting rather than the rising sun. American multinational activity reached its peak in the mid 1960's; and in examining legislation aimed at foreign direct investment, and the surrounding literature, it soon becomes clear that such legislation was initially and primarily an attempt to check the strong current of inflowing *American* investment. There is nothing astonishing about that. The U.S. at that time was indisputably the largest - if not the only significant - source of massive foreign direct investment. The tide, however, has turned. The flow of foreign direct investment in the industrialized world is now stronger in the east-to-west direction and the 'Problem' of control is thus, in part, taking care of itself by virtue of the investment flow seeking and establishing its own equilibrium, largely through protected and strengthened competition from Europe, where economic recovery from World War II was inevitably slower than in the United States, but which caught up surprisingly rapidly, due largely to the boost from American post-war aid programmes.

This turning tide, or more precisely to pursue the image, this 'undertow'[4] (as the outward flow from, for example, Europe is, to a large degree, a result of the inward flow, and very strongly reliant upon it for its own outward pull) was already gathering momentum in the early 1970's, and has only recently been given a mammoth stimulus by the more advantageous exchange on the U.S. dollar, the full implications of which cannot yet be calculated.

Thus, having asserted that the control of the multinational *per se* in the industrialized world: (1) is not, or (2) is no longer, effectively a Problem, but rather an Issue within which identifiable problems can and do arise, presenting a continuous challenge to legislators, government officials and lawyers alike, but, in the main, resolvable through the normal judicial and governmental

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American Academy of Political and Social Science, Vol. 403, September 1972, at 64-65.

3. Behrman, "The Multinational Enterprise and United States Foreign Economic Policy", 52 *Indiana Law Journal* (1977), at 614.

4. "...the current beneath the surface that sets seaward...when waves are breaking upon the shore" (*Webster's New Collegiate Dictionary* [1977]).

processes, it must nonetheless be conceded that the current movement toward international controls did not originate spontaneously, and cannot be ignored. While the fears which arise within the host society tend to be primarily confined to the affiliated company's direct (or indirect) effects upon the individual host state, and the presumed threat to its sovereignty, even if such a threat is more imaginary than real, in one sense a Problem exists if only from the mere fact that one is seen to exist. Fears are real; and that indeed in itself constitutes a Problem. The fears primarily generated by the reverberations of the earlier explosive expansion in the 1960's have mostly proved groundless, or have since become outdated. And as one author writing in 1972 expressed it:

> When the present dispute between sovereignty and multinationalism subsides, and the dust settles down, a better reciprocal understanding will hopefully emerge, and most of the mistrust, doubts, and fears which have been expressed of late will vanish. This writer firmly believes that there is no case for an irremediable conflict between sovereignty and multinationalism. The alleged tensions between them are neither basic nor permanent, but they are rather the result of psychological reactions to spotty instances.[5]

Fears must be replaced by facts. One of the principal functions of the United Nations Center on Transnational Corporations has been the undertaking of a widespread fact- and information-gathering campaign which will hopefully alleviate apprehensions of the undisclosed. In the present work, an attempt will also be made to replace some of the questions regarding the existence or non-existence of controls by fact. The basic issues of control dealt with herein are approached through a systematic exploration of major legal responses to the fears as well as to actual instances of abuse - i.e. the legal techniques used, nationally and transnationally, to effectively control multinational activities from the moment of the MNE's application for entry into the host economy, through the entire duration of MNE operations within the host jurisdiction, to the moment - if that moment ever arrives - of expulsion (or expropriation) of the foreign enterprise by the host government.

This, then, is the main direction of the present study, namely, whether those existing legal techniques enumerated - or other potential legislation envisaged for application within the national legal framework - are sufficient to control, in practice, the MNE in all its operations, to an extent accepted as reasonable; or whether an international regime is required, in addition, in order to attain

5. Rogers, op cit., *supra* note 2, at 65.

the degree necessary and adequate for ensuring that any excesses or abuses on the part of the MNEs be minimized, while at the same time taking care to safeguard and maximize their recognized benefits to the host economies.

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