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An Emerging International Framework for Transnational Corporations

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Peter Hansen and Victoria Aranda

Abstract

The emergence of the transnational corporation (the “TNC”) as a main engine of global economic activity is a phenomenon characteristic of the post-Second World War period. These corporations revolutionized international business patterns, leading to an unprecedented level of transnationalization of the world economy. The importance of foreign investment and TNC activity in the world economy is best illustrated by the following figures: after a period of about five years of steady growth, in 1989 outflows of foreign direct investment reached a level of US\$196 billion, while the total stock was US\$1.5 trillion. Recent estimates suggest that, for a number of large developed economies, about ninety percent of technology payments occur through transnational corporations. For the United States, about eighty percent of its international trade takes place within TNCs, of which about forty percent is intra-company trade. At the same time, cross-border corporate strategies and complex inter-corporate alliances are making the identification of a single nationality for a TNC increasingly difficult..... But the nature of the transnational corporation as a group of enterprises with a unified structure and with common control and strategy has yet to find a legal regime that matches those characteristics..... One of the first works that looked into the possibilities of establishing an international regime for transnational corporations was the survey of transnational corporations in world development, which led to the creation of the Commission and the Centre on Transnational Corporations, which I now represent. But it soon became obvious that the establishment of such a regime would encounter major difficulties, as it would have to reconcile the global economic “realities” of a TNC-dominated economic system with the need to safeguard the sovereignty and economic independence of the state as a fundamental entity of the political system, and especially of the most vulnerable among states, the developing countries.

ADDRESS

AN EMERGING INTERNATIONAL FRAMEWORK FOR TRANSNATIONAL CORPORATIONS

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The emergence of the transnational corporation (the "TNC") as a main engine of global economic activity is a phenomenon characteristic of the post-Second World War period. These corporations revolutionized international business patterns, leading to an unprecedented level of transnationalization of the world economy. The importance of foreign investment and TNC activity in the world economy is best illustrated by the following figures: After a period of about five years of steady growth, in 1989 outflows of foreign direct investment reached a level of US\$196 billion, while the total stock was US\$1.5 trillion. Recent estimates suggest that, for a number of large developed economies, about ninety percent of technology payments occur through transnational corporations. For the United States, about eighty percent of its international trade takes place within TNCs, of which about forty percent is intra-company trade. At the same time, cross-border corporate strategies and complex inter-corporate alliances are making the identification of a single nationality for a TNC increasingly difficult. Thus, International Business Machines and Hewlett-Packard (US) are locating key corporate functions in Western Europe, while Honda and Nissan, the Japanese automobile manufacturers, are becoming important exporters for the United States.¹

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** Transnational Corporations Affairs Officer, U.N. Centre on Transnational Corporations, New York. In the preparation of this Article, the Authors have drawn on a number of materials published by U.N. Centre on Transnational Corporations (the "UNCTC") over the years.

1. See UNCTC, *TRANSNATIONAL CORPORATIONS AND INTERNATIONAL ECONOMIC RELATIONS 1991: THE TRIAD IN FOREIGN DIRECT INVESTMENT—IMPLICATIONS FOR DE-*

But the nature of the transnational corporation as a group of enterprises with a unified structure and with common control and strategy has yet to find a legal regime that matches those characteristics. From the legal perspective, a transnational corporation is only recognized as a group of separate national companies established under the laws of different countries. The lack of a truly international system for transnational corporations has been blamed by some theorists for depriving those corporations of their ability "to pursue the true logic of the global economy," as Mr. George W. Ball put it in his seminal article,² and believed by some other scholars to be an impediment for maintaining effective control over their operations, and making it difficult or impossible to hold the entire enterprise accountable for its actions.³

One of the first works that looked into the possibilities of establishing an international regime for transnational corporations was the survey of transnational corporations in world development,⁴ which led to the creation of the Commission and the Centre on Transnational Corporations, which I now represent. But it soon became obvious that the establishment of such a regime would encounter major difficulties, as it would have to reconcile the global economic "realities" of a TNC-dominated economic system with the need to safeguard the sovereignty and economic independence of the state as a fundamental entity of the political system, and especially of the most vulnerable among states, the developing countries. Indeed, while other international business transactions usually involve one-time operations at the border, foreign direct investment and TNC operations penetrate deeply into the national fiber of the host country and also presuppose a long-term relationship with that country. Consequently, while it was a relatively easy task to adopt global instruments setting up international regimes to deal with trade, finance, and mone-

VELOPING COUNTRIES (forthcoming publication). This UNCTC study analyzes recent trends in foreign direct investment.

2. Ball, *Cosmocorp: The Importance of Being Stateless*, 2 (No. 6) COLUM. J. WORLD BUS. 25 (1967).

3. See, e.g., Burchill, *The Multi-National Corporation: An Unsolved Problem in International Relations*, 77 QUEENS Q. 3 (1973).

4. U.N. DEP'T OF ECONOMIC AND SOCIAL AFFAIRS, MULTINATIONAL CORPORATIONS IN WORLD DEVELOPMENT, U.N. Doc. ST/ECA/190, U.N. Sales No. E.73.IIA.11 (1973).

tary matters, the conclusion of a similar instrument for foreign direct investment and TNC activity has proven to be more elusive.

*THE EXISTING INTERNATIONAL FRAMEWORK OF
FOREIGN DIRECT INVESTMENT*

The international framework of foreign direct investment ("FDI") as it exists today is mainly the cumulative result of a number of instruments that have been adopted at different times, most of them during the last forty years. Those instruments present different characteristics, both in terms of their structure, scope, approach, and content, and their legal nature and underlying philosophy. They reflect the changing moods, perceptions, and expectations of governments with respect to transnational corporations in response to rapidly evolving and dynamic international economic conditions and relations.

One of the main preoccupations of the developed countries with respect to foreign investment over the years has been to secure international standards for the protection of their investments abroad. The existence of conflicting doctrines with respect to the role of international law in the area of foreign investment, as well as the uncertainty about the specific content of international customary law rules regarding the protection of private property abroad, has led those countries to take various initiatives, first at the multilateral level, aimed at establishing international agreements on the treatment of foreign investments. Starting with the Havana Charter,⁵ which contained a number of important provisions on investment, and continuing with the OECD draft convention for the protection of foreign investments,⁶ most multilateral attempts to adopt general, legally-binding standards for the treatment of investors have been inconclusive. However, not all efforts were unsuccessful: A multilateral agreement was possible, as early as 1965, on the very critical and rather controversial issue of the

5. Charter for an International Trade Organization (Mar. 24, 1948), *reprinted in* U.N. Doc. ICITO/1/4 (1948) *and in* U.S. DEP'T OF STATE, Pub. No. 3206, Commercial Policy Series No. 114 (1948).

6. Organisation for Economic Co-operation and Development ("OECD"), Draft Convention on the Protection of Foreign Property and Resolution of the Council of the O.E.C.D. on the Draft Convention, OECD Pub. No. 23081 (1967), *reprinted in* 7 I.L.M. 117-43 (1968).

settlement of investment disputes between states and nationals of other states.⁷

In view of those difficulties, a number of major developed countries turned to the bilateral level in order to provide legal protection under international law to their investments in developing countries.⁸ The number of bilateral treaties for the promotion and protection of foreign investments has been growing steadily in the last few decades, and new countries have joined in this practice. However, despite their growing numbers and their similarity, it is doubtful that bilateral investment treaties, in and of themselves, can amount to a global statement of customary international law on the protection of foreign investors, as many authors have maintained.⁹ Those who question the custom-forming effects of bilateral investment treaties have argued, among other things, that bilateral investment treaties are concluded in the context of a special economic and political bilateral relationship, often bundled with a number of mutual concessions on a reciprocal basis.¹⁰

The standards of treatment prescribed in most bilateral treaties include fair and equitable treatment, national and most-favoured-nation treatment, as well as a number of specific protection standards on expropriation, transfer of payments, and settlement of disputes. With respect to entry and establishment of foreign investors, the position of classic customary international law has been that states have the right to regulate these matters, and, more specifically, to determine the role that such investments play in their economic and social development, and thus to prohibit or limit the extent of their presence in specific sectors. This approach has been maintained in most bilateral investment treaties.¹¹ Nevertheless, in

7. Convention on the Settlement of Investment Disputes Between States and Nationals of Other States (Oct. 14, 1966), 17 U.S.T. 1270, T.I.A.S. No. 6090, 575 U.N.T.S. 159.

8. See UNCTC, *BILATERAL INVESTMENT TREATIES*, U.N. Doc. ST/CTC/65, U.N. Sales No. E.88.II.A.1 (1988) [hereinafter *BILATERAL INVESTMENT TREATIES*]. This document analyzes the treaties in detail.

9. See, e.g., Mann, *British Treaties for the Promotion and Protection of Investments*, 52 *BRIT. Y.B. INT'L L.* 241 (1981). Mr. Mann is one of the supporters of the custom-forming theory. See *id.*

10. See, e.g., Schachter, *Compensation for Expropriation*, 78 *AM. J. INT'L L.* 121 (1984).

11. See *id.*; see also *BILATERAL INVESTMENT TREATIES*, *supra* note 8.

the context of some regional schemes, developed countries in particular have gradually introduced the concept of freedom of entry and establishment for foreign investments.

Another important aspect of the framework for TNCs relates to the standards of behaviour expected from those corporations in their operations outside their home countries. Some of the most significant initiatives in this regard were taken during the 1970s, as awareness of the economic power and influence of transnational corporations intensified both in developing and developed countries. Developing countries in particular viewed the growing expansion of TNCs from the old colonial powers as a potential threat to their newly-attained political independence. Many of those concerns were also shared by trade unionists, consumers, and other public opinion groups in developed countries. The developing countries, with the support of those groups, initiated a number of efforts in the United Nations. Some of those initiatives were generally aimed at restructuring the international economic order, and in that context called for, among other things, the "regulation and supervision of the activities of transnational corporations in the interest of the national economies of the countries where such transnational corporations operate on the basis of the full sovereignty of those countries."¹²

Other efforts in the United Nations concentrated on the elaboration of international standards to deal with specific aspects of the activities of transnational corporations. Thus, in the area of employment and labor relations, the International Labour Organisation adopted the Tripartite Declaration of Principles Concerning Multinational Enterprises and Social Policy.¹³ The declaration addresses governments, employers, and workers' organizations as well as transnational corporations, and sets out a number of voluntary standards in the areas of employment, training, conditions of work and life, and industrial relations. Another important instrument adopted within the aegis of the U.N. Conference on Trade and Development ("UNCTAD") was the Set of Multilaterally Agreed Eq-

12. DECLARATION OF THE ESTABLISHMENT OF A NEW INTERNATIONAL ECONOMIC ORDER, G.A. Res. 3201 (S-VI), 6 U.N. GAOR Supp. (No.1), U.N. Doc. A/9559 (1974).

13. 17 I.L.M. 423-31 (1978).

uitable Principles and Rules for the Control of Restrictive Business Practices,¹⁴ which provides a number of principles and guidelines for identifying and dealing with situations where there is abuse of a dominant position of the market. On the question of illicit payments, efforts by an international working group within the aegis of the Commission on Transnational Corporations resulted in a complete draft agreement, which, however, was never formally adopted by the General Assembly. Moreover, in the crucial area of transfer of technology, work on a code of conduct within the aegis of UNCTAD has also led to an advanced draft that spells out, for the first time, important international standards on this issue,¹⁵ though there are still some outstanding issues to be resolved before the draft code can be formally adopted.

The most far-reaching attempt so far to establish international standards on issues relating to transnational corporations, both in terms of its comprehensiveness and its universal scope, has been the elaboration of a U.N. Code of Conduct on Transnational Corporations (the "Code").¹⁶ The Code includes both standards for the activities of transnational corporations as well as standards for the treatment of those corporations by their host countries. The standards of corporate behaviour cover a wide range of legal, economic, political, and social issues. These standards are based on the recognition of the sovereign authority of the state over foreign investment within its jurisdiction, but also on the need for international cooperation to deal with the full implications of the operations of transnational corporations across national borders. This approach was reflected mainly in provisions dealing with non-interference in internal affairs of host countries, permanent sovereignty over natural resources, and adherence to development objectives and policies of host countries. On the basis of those general principles, it has been also possible to elaborate

14. U.N. Doc. TD/RBP/CONF/10 (1980), U.N. Sales No. E.81.II.D.5, *reprinted in* 19 I.L.M. 813-23 (1980).

15. U.N. ECONOMIC & SOCIAL COUNCIL, DEVELOPMENT AND INTERNATIONAL ECONOMIC COOPERATION: TRANSNATIONAL CORPORATIONS, U.N. Doc. TD/CODE TOT/41 (1983).

16. U.N. CONFERENCE ON TRADE & DEVELOPMENT (UNCTAD), DRAFT INTERNATIONAL CODE OF CONDUCT ON THE TRANSFER OF TECHNOLOGY, U.N. Doc. E/1990/94 (1990).

more specific provisions in the Code in a number of concrete areas, such as parent-affiliate relations, disclosure of information, and consumer and environmental protection.

The provisions of the Code on the treatment of transnational corporations by their host countries include several general standards, notably, fair and equitable treatment and national treatment, as well as specific standards on issues such as nationalization and compensation, transparency of national regulation, transfer of payments, settlement of disputes, conflicts of jurisdiction, and conflicting requirements. Moreover, the Code includes an umbrella clause with a general reference to international law or international obligations as the overall measure for the treatment of transnational corporations.

The formulation of general standards for corporate behaviour was a relatively easy task, and by 1982, most provisions in this area were agreed *ad referendum*. Since then, the negotiations on the Code concentrated on the resolution of a number of outstanding issues, mainly in the section dedicated to the treatment of transnational corporations. In recent years, there has been a remarkable degree of progress on the formulation of standards on some of the issues that only a few years ago appeared intractable, such as the definition of transnational corporations—that is, whether the Code would apply to state corporations, the principle of fair and equitable treatment, the elaboration of a principle of non-interference in internal affairs of the host countries as it relates to transnational corporations, and the formulation of the standard of compensation upon nationalization of foreign property. On other issues, such as the reference to international law, settlement of disputes, and national treatment, some differences persist but compromise formulations have been found that would seem to accommodate the concerns of most countries.

While efforts continue towards the completion of the global Code, governments have recently taken an additional step towards the protection of investments with the establishment of the Multilateral Investment Guarantee Agency (“MIGA”)¹⁷ under the aegis of the World Bank. MIGA’s main role is to provide insurance coverage for non-commercial risks

17. Convention Establishing the Multilateral Investment Guarantee Agency, 24 I.L.M. 1605-38 (1985).

involved in transnational investments, and therefore it does not pretend to enunciate substantive standards for the treatment or the activities of foreign investors. But in making its underwriting decisions, MIGA would need to draw from international standards in other instruments in order to determine both the contribution of a particular investment project to the development of the relevant host country, and the appropriateness of the standards of protection offered by that country. In that respect, MIGA and the Code can be seen as mutually complementary instruments.

Another major multilateral initiative in recent years was the new round of trade negotiations under the aegis of the General Agreement on Tariffs and Trade (the "GATT").¹⁸ While the Uruguay Round is primarily concerned with trade issues, it is also expected to have major implications for foreign investments in the future, particularly the negotiations on trade in services and on trade-related investment measures ("TRIMS"). The main objective of the Uruguay Round is to strengthen and expand the system of free trade advocated by GATT to cover new areas, such as services, and new issues, such as certain investment measures, which were not included in previous GATT instruments.

Significant progress was also made in the past decade in the elaboration of international standards on issues and activities closely related to transnational corporations through the adoption of a number of issue-specific instruments, some of which have already gone beyond the standards proposed in the global Code. Thus, the completion of an International Code of Marketing of Breast-Milk Substitutes¹⁹ in 1981 under the aegis of the World Health Organization was followed a few years later by the adoption of a set of Guidelines of Consumer Protection²⁰ by the U.N. General Assembly. But it is perhaps in the area of the protection of the environment where most efforts have been concentrated in recent years, as awareness of the imminent threat of a rapidly deteriorating environment

18. Oct. 30, 1947, 61 Stat. pts. (5) & (6), T.I.A.S. 1700, 55 U.N.T.S. 308.

19. See WORLD HEALTH ORGANISATION, *THE INTERNATIONAL CODE OF MARKETING BREAST-MILK SUBSTITUTES: SYNTHESIS OF REPORTS ON ACTION TAKEN (1981-1990)*, U.N. Doc. WHO/MCH/NUT/90.1 (1990).

20. U.N. DEP'T OF INT'L ECONOMIC & SOCIAL AFFAIRS, *GUIDELINES FOR CONSUMER PROTECTION*, U.N. Doc. ST/ESA/170, Sales No. E.86.IV.2 (1986).

grows in all countries. Given the crucial role played by transnational corporations in the development and transfer of new products and technologies and to developing countries, the U.N. Commission and Centre on Transnational Corporations recently elaborated a set of Criteria for Sustainable Development (the "Criteria").²¹ The Criteria are aimed at encouraging corporate management in their investment decisions to make a positive contribution to sustainable development by maintaining economic growth while reducing environmental risk and resource over-exploitation.

Another aspect in which significant progress has also been possible in recent years concerns the elaboration of international standards on accounting and reporting, mainly as a result of the work of a number of international institutions, including the Intergovernmental Group of Experts ("ISAR") established under the aegis of the Commission and the Centre on Transnational Corporations. Indeed, as one of the very few groups that incorporates developing as well as Eastern European countries in its membership, ISAR has contributed to the harmonization of accounting standards in those regions. Thus, ISAR has recently undertaken work on a number of new issues, such as environmental accounting, accounting for joint ventures, and developing accounting standards for the Eastern and Central European economies.

*CONCLUSION: AN INTERNATIONAL APPROACH TO
FOREIGN DIRECT INVESTMENT FOR THE
FUTURE*

A summary review of some of the main instruments dealing with foreign direct investment is indicative of the changes that have taken place in governments' perceptions about the role of TNCs in economic development over the years. Thus, while efforts towards securing internationally agreed standards for the protection of foreign investments have continued during the last four decades, the need to address the full implications of the operations of TNCs across national borders became a priority for developing countries since the 1970s, and, at least for a while, seemed to overshadow other considerations, leading to the call for elaboration of international stan-

21. UNCTC, CRITERIA FOR SUSTAINABLE DEVELOPMENT MANAGEMENT (1991).

dards for the activities of TNCs. In the last decade, there was a renewed emphasis on the protection and encouragement of investments in international discussions, but those discussions have also revealed continuing problems in TNC/host country relations. The result is perhaps a more balanced approach to TNC issues and discussions at the multilateral level.

These changing moods have also been reflected in the negotiations on the Code. Thus, after an initial period of success in the elaboration of the standards of conduct for TNCs, the negotiations stagnated for a while as a number of outstanding issues in the area of treatment made progress difficult. In the last few years, renewed efforts by Western countries at formulating standards in the area of treatment of foreign investors are meeting a more receptive response from developing countries, and also from the Eastern and Central European nations, than in previous decades. At the same time, the progressive elaboration of standards on the activities of TNCs help establish a balance between the obligations and rights of states and transnational corporations.

The increasing transnationalization of economic activity and the recent changes in international economic relations have emphasized the central role TNCs play in mobilizing resources across national borders. Those developments have also enhanced the need for strengthening intergovernmental cooperation in the area of foreign direct investment through, among other things, the establishment of appropriate international instruments that match the global reach of TNC operations.

The improved investment climate in most countries provides the appropriate background for concluding a global instrument on foreign direct investment which includes all countries and regions of the world. Such an instrument would need to be negotiated and adopted within a worldwide organization to ensure that the standards stated therein apply to worldwide economic relations. The instrument should encompass existing arrangements and build upon principles already accepted. It should address both governments and TNCs, and should set out in a balanced manner the rights and responsibilities of all parties to an investment relationship.

The Code, now near completion, meets all these charac-

teristics. Therefore, its completion would give expression to major parts of the existing international framework on transnational corporations and provide a broad basis for further elaboration of international standards in the future.