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WORK RELATED TO THE CODE OF CONDUCT ON TRANSNATIONAL CORPORATIONS
AND OTHER INTERNATIONAL ARRANGEMENTS AND AGREEMENTS: CODE OF
CONDUCT ON TRANSNATIONAL CORPORATIONS

Progress made in the work on the code of conduct on
transnational corporations

Report of the Secretary-General

SUMMARY

Informal consultations on the code of conduct intensified during the past year. They were preceded by a symposium at which a number of personalities in the field of international economic law suggested some prescriptions for the resolution of the outstanding issues in the code. The outcome of that effort is discussed in the first part of this report.

Since negotiations on the code were initiated in 1976, there have been a number of significant developments affecting the economic and political environment for the code negotiations. Those encompass an array of macro-economic changes which emphasize the linkages between trade, investment and financial issues, leading to a more integrated policy approach to related issues. As a major organizational vehicle for this integration, transnational corporations must of necessity be a focal point in current policy considerations. The new policy dynamic stresses the need for an international framework to address the essential economic functions performed by these corporations.

* E/C.10/1990/1.

At the same time, changing foreign direct investment patterns have altered the traditional geo-political pattern of home and host country roles, laying the basis for similar alterations in their outlook of specific transnational corporation issues still being debated in the code negotiations.

The impact of change and the opportunities for a successful conclusion of the code negotiations found in the new investment environment are examined in the second and third part of this report, the latter focusing on the interrelationships between the Code and the Uruguay Round of Multilateral Trade Negotiations on services. An evaluation of the main findings in these sections leads to the conclusion that the draft code provides the appropriate framework to deal effectively with current and emerging transnational corporation issues in the new policy environment.

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INTRODUCTION

1. As its fifteenth session, the Commission on Transnational Corporations requested the United Nations Centre on Transnational Corporations to prepare a report for its sixteenth session on the status of the negotiations on the code of conduct on transnational corporations. The present report has been prepared in response to that request.
2. Chapter I reviews the progress made on the code negotiations since the last Commission session. Chapter II analyses a number of recent developments in international economic relations involving foreign direct investment, and their impact on the code negotiations. Chapter III considers the interrelationships that exist between the code of conduct and the Uruguay Round of Multilateral Trade Negotiations, and how those negotiations may facilitate the conclusion of the code. In the concluding part, the prospects for an early conclusion of the code are discussed in the light of the findings of the proceeding sections.

I. PROGRESS ON THE CODE NEGOTIATIONS

3. In resolution 1989/24 the Economic and Social Council, endorsing a consensus proposal by the Commission, reaffirmed the need to finalize the code of conduct on transnational corporations as soon as possible, and requested the Chairman of the special session of the Commission on Transnational Corporations, in co-ordination with the Executive Director of the United Nations Centre on Transnational Corporations, to intensify consultations with the view of resuming negotiations on the code in the context of the special session of the Commission, possibly no later than the end of 1990. Pursuant to that resolution, a number of efforts were undertaken aimed at facilitating a decision on the resumption of formal negotiations on the code.
4. A group of eminent personalities in the field of international economic law gathered at the Peace Palace, the Hague, on 15-16 September 1989 for a symposium on the outstanding issues in the code of conduct. The purpose of the symposium was to facilitate constructive discussions among high-level international experts, with the aim of assisting the Commission in the negotiation of those issues. An important task for the group was to review the outstanding issues in the light of recent State practice, decisions of international tribunals, treaties and other sources of international law; to determine the status of evolution of international law in the relevant areas; and to suggest ways in which the interaction between international law, national law and the code instrument could facilitate the formulation of the code standards. The participants noted several recent changes in the economic scene of relevance to the code. To most observers, the developments have rendered the need for the code - that is, a global, comprehensive and balanced framework on foreign direct investment and transnational corporation activity - more acute than before, because they emphasize the growing significance of transnational corporations in the world economy and increase the importance of concluding international standards to guide essential economic functions undertaken by those corporations. It was also stressed that the fundamental need for the

international community to address the consequences of the operations of transnational corporations by international standards to supplement national law in that area has not changed. With respect to the outstanding issues, it was generally felt that agreement on the code was likely to be found by means of flexible formulations that accommodate different views rather than on the basis of the legal merits of one or another alternative. There were not strong objections to the present formulations in the code, and, in the view of most commentators, the present format of the code was feasible. The participants made a number of suggestions on specific outstanding issues. These are reflected in the report on the symposium, which is reproduced in the annex below.

II. A CHANGING INVESTMENT ENVIRONMENT

5. Last year's report to the Commission on the code of conduct outlined a number of recent developments in international economic conditions and relations of relevance to the code. Those developments and their implications for current code discussions have been further analysed in a recent study prepared by UNCTC. 1/ The main findings of that study are summarized in the present report.

6. The birth of numerous independent and sovereign States and the expansion of transnational corporations in the period after the Second World War gave impetus to the debate on a code of conduct for transnational corporations. Support for the code emerged primarily in the developing world but also in the industrialized home countries of transnational corporations, particularly in academia and among the ranks of organized consumer, environmental and labour groups. In the case of the latter, fear of job loss through transfer of plants abroad raised intense and active interest in the elaboration of standards on corporate responsibility, concerning, in particular, information disclosure and labour management relations for transnational corporations. These and other concerns of a transnational nature, such as the discovery of widespread use of illicit payments by transnational corporations to obtain business abroad, led some of the major industrialized countries in that early period to press for international standards for foreign investment at the United Nations. The Intergovernmental Working Group entrusted with the preparation of the code reached tentative agreement, in a very short time, on the large majority of the provisions of the draft code, including most of the provisions in the section dedicated to the behaviour of transnational corporations. Later, efforts by the Commission led to agreement on the definition of transnational corporations and to substantial progress on the treatment issues, notably on non-interference in internal host country affairs; fair and equitable treatment standards for corporations; jurisdiction, settlement of disputes and transparency of national norms. While the Commission on Transnational Corporations proceeds with the negotiation of the outstanding issues in the draft code, progress has occurred on a wide range of specific instruments relating to transnational corporations. Numerous other international negotiations are under way, covering a wide range of functional and sector-specific issues.

A. Recent changes of relevance to the code

1. Macro-economic changes

7. Important macro-economic changes since the mid 1960s have shaped the nature of international policy issues in the current global system. International trade dominated the early period, but rapid transnational corporation expansion progressively tied national economies together and laid the foundation for an interdependent international economy. Investment issues joined trade concerns on the international agenda during the 1970s, as petro-dollar recycling and the collapse of the Bretton Woods system introduced new international monetary concerns. New financial issues emerged in the 1980s when the debt crisis and currency realignments became a focus of increasing public interest and concern. These phenomena are related in many complex ways. The macro-economic context in which these issues had to be considered linked together questions relating to trade, investment and the management of monetary aggregates. Against that background the rigid categories used in the past on the analysis of policy issues have proved inadequate, and the development of a more appropriate policy dynamic has required a new synthesis. In searching for that synthesis, the activities of transnational corporations have been a focal point, drawing together through their day-to-day activities many disparate strands of policy. In that context the international community looking at the interplay of those policy issues may need a normative framework as a yardstick or gauge.

8. The relevance of this more integrated policy environment for transnational corporation-related issues is suggested by the emergence of such new mechanisms as debt-to-equity swaps, whose financial benefits may be contingent on assurances that the resulting direct investments will yield trade-generated foreign exchange earnings. New interrelationships are also evident in debates about investment regulations that govern trade in services, or the effects of so-called trade-related investment measures (TRIMs) that often involve governmental incentives and disincentives covering a range of trade, investment and financial policies.

9. Another development that reflects the growing policy linkage between trade, investment and monetary issues is the broader integration occurring in regional economic zones. The European Community, initially a common market that developed around a co-ordinated trade policy, is moving rapidly towards an internal market reform that will force a more common approach to the treatment of investment and stimulate further progress on monetary policy and fiscal co-ordination. The recently concluded Free Trade Agreement between the United States and Canada is far more than a trade accord, merging into cross-border investment policies that shape business conditions in an increasingly integrated market where monetary movements are already functionally linked.

10. Of special relevance for this increased linkage between macro-economic policies is the integrative role played by transnational corporations, which incorporate trade, investment and monetary dimensions in their daily operations. Organized through the vehicle of foreign direct investment, transnational corporations channel global private financial flows through their networks, either

ancillary to manufacturing operations or as part of the rapidly expanding realm of transnational corporation service enterprises. The major portion of world trade also flows within, between or among transnational corporations. Recent figures show that between 30 and 40 per cent of the trade of several major developed countries is intra-firm - that is, it occurs within a transnational corporation's affiliate network. After adding interfirm transactions, transnational corporations account for over three fourths of the countries' total international trade. 2/

2. Changing investment patterns

11. The average annual growth rate of world foreign direct investment outpaces both global merchandise exports and world economic output. Total world stock of foreign direct investment increased from \$519 billion in 1980 to \$1,023 billion by the end of 1987. 3/ Within this general expansion, significant changes are occurring in the national origin and destination of new foreign direct investment, thereby altering the make-up and distribution of the transnational corporation community. These trends foster accompanying changes in the traditional geo-political pattern of home and host country roles, particularly among the developed countries, laying the basis for similar alterations in their policy outlook on specific transnational corporation issues.

12. The United States, historically the world's top supplier of direct investment capital and home to the largest number of transnational corporations, has attracted progressively larger inflows of direct investment funds. 4/ As a result, that country now plays host to approximately as much direct investment from other countries as United States-based transnational corporations have invested abroad. Conversely, Western Europe has maintained, over the 1970s and 1980s, a roughly balanced position as both a supplier and recipient of foreign direct investment. The trend might now be affected by the recent pick-up of investments in Europe as corporations seek to position themselves in anticipation of the implementation of European Community internal market reforms in 1992. 5/ Investment patterns are shifting in Canada as well, long viewed as an atypical developed country in that it was concerned primarily with the policy problems of a host country. Canada's relative shares of the world stock of inward and outward direct investment had narrowed from 18.2 per cent and 3.3 per cent in 1962 to 8.5 per cent and 4.5 per cent in 1987, moving the region towards a position of greater balance between inward and outward direct investment. 6/

13. Japan is the major developed country that is now most dramatically out of balance in terms of a home/host country relationship. But Japan's role is still relatively new. The first major outflow of foreign direct investment from Japan began in the early 1970s and grew rapidly over the 1980s. Now Japan is also beginning to face greater inward direct investment. Policy pressures forced a lowering of barriers early in the 1980s, and transnational corporations from Europe and the United States are responding by seeking to establish a market position within the growing Japanese economy. 7/

14. These developments suggest a balancing trend among developed countries where cross-investments may create the basis for a more common policy outlook. The United States, especially, now grapples with issues of increased foreign ownership in its economy rather than promoting only home country positions. Meanwhile Japan already faces reciprocity demands, especially in the service sectors, that will limit its investment abroad unless a corresponding foreign investor presence is accepted there. 8/

15. The most persuasive explanation for this expanded cross-investment pattern is the greater parity that now exists between the world's developed regions. Corporations find they must be physically present in all areas in order to compete, particularly to stay abreast of new technological developments and to engage in a broad enough marketing campaign to recover the spiraling costs of research and development efforts. The forces of technological change have overtaken the widely accepted product life-cycle theory that explained much of the early foreign direct investment in manufacturing industries, especially those originating in the United States in the 1960s and into the 1970s. Now, competitive pressures from rapid technological innovation have compressed the theory's hypothesized time sequences to such a degree that the phased trade and investment decisions of the past are no longer possible. 9/

16. On the other hand, foreign investment to developing countries has stagnated, concentrating itself in a handful of relatively advanced industrializing countries. The developing world's share of direct investment stock dropped from over 30 per cent in 1967 to roughly a one quarter share in the 1970s and early 1980s. Well over three fourths of foreign direct investment flows in the 1980s moved among countries of the Organisation for Economic Co-operation and Development (OECD), while some 86 per cent of the remainder went to only 18 developing countries and territories. This uneven distribution is accounted for by the concentration of foreign direct investment in countries that have abundant natural resources, large domestic markets and/or abundant skilled but still relatively low-cost labour. While over one half of the total inward stock of foreign direct investment in developing countries is in the western hemisphere, the fastest annual growth rates occur in a few rapidly industrializing Asian countries. 10/

17. Technological change also accounts for some of the reduced attractiveness of many traditional host and other developing countries to foreign investors. Discoveries in new materials and processes lower demand for many of the raw materials traditionally supplied by developing countries. Automation and quality-control requirements make unskilled and semi-skilled labour a relatively less important component of manufacturing costs, decreasing the advantage of locating operations in labour-surplus countries. Few developing countries offer the range of knowledge-intensive skills or educational infrastructure necessary to compete as sites for information technology firms.

18. While losing these advantages on the production side, most developing countries also lack large enough internal markets to justify local production sites based on final sales figures. In fact, as cross-investment brings new threats to transnational corporation home markets, corporations concentrate their resources even further at home to battle foreign competitors for shares in major established markets, rather than exploring new market potential in the developing world.

19. This altered foreign direct investment pattern suggests the emergence of a technological convergence in the world's leading industrialized countries, and perhaps a small group of advanced developing or newly industrializing countries which are positioned to make similar progress. ^{11/} Among these countries, cross-investment trends will lead to more balanced policy positions between home and host country outlooks on foreign investment issues. The vast majority of other countries face an increasing gap between themselves and the industrialized countries, and the risk of being relegated on foreign investment issues to the position of an expectant but usually ignored suitor. While not dictating the flow of all foreign direct investment, the key factors of technological innovation, cross-investment competition and internal market size now appear to determine the location of new investment for traditional manufacturing transnational corporations as well as probably for service sector firms.

20. These competitive dynamics and their impact on geo-political alignments establish part of the environment for code discussions. Developed countries face a stronger imperative than in the mid 1970s to strengthen international co-operation on investment-related issues and their more balanced cross-investment positions may forge enough common ground to achieve positive results.

3. Changes in transnational corporations

21. In the mid to late 1970s, transnational corporations began a metamorphosis that both responds to and reinforces global macro-economic and technological change. Many of these changes are reflected in shifting aggregate investment trends but incorporated within the evolution of individual transnational corporation structures and operations. In several fundamental respects, the transnational corporation universe has also changed. Transnational corporations now come in all shapes and sizes from many different countries, supplying an evolving array of products and services through complex but fluid business arrangements. These changes diffuse power in many transnational business networks and weaken the ability of single national Governments to direct and control the full impact of transnational corporation activities.

(a) Changing numbers and sectors

22. Available statistics do not allow precise calculations, but some conclusions are possible with regard to the changes in the composition of transnational corporations. Some 600 firms are now part of a "billion dollar club" that generates roughly 20 per cent of total value-added in manufacturing and agriculture, although about 70 large transnational corporations account for one half of the sales. Twenty years ago, some 60 transnational corporations accounted for 50 per cent of the foreign direct investment total. Those figures have not changed much, but the composition of the club is now different. Corporations based outside the United States increased their representation among the top dozen or so firms in key product sectors, reflecting the diffusion of economic power and a more diversified competitive structure. The large number of small to medium-sized firms that invest abroad appear to move first into similar developed countries. These smaller transnational corporations appear to be growing in the degree of their

global involvement, while the ratio of foreign to domestic sales among larger transnational corporations has remained roughly the same. 12/

23. Several Eastern European countries, as well as China and the Soviet Union, additionally took historic steps to open their economies to a controlled inflow of foreign direct investment. In early 1989, nearly 200 joint ventures were reported in the USSR. 13/ But the number of joint ventures appears to be growing every day. According to recent estimates, by September 1989 more than 900 joint ventures had been registered in the USSR 14/ and by 1990 some 1,000 joint venture agreements are expected to have been signed. 15/ In Poland, the number of joint ventures registered by September 1989 are estimated to be about 1,330 (including some 800 "Polonia" firms), 16/ and in Hungary about 600. 17/ These actions suggest that group D countries will play a more active part in the consideration of foreign direct investment issues in future United Nations discussions and offer the possibility for expanded common ground to the extent that these countries act as both home and host locations.

24. The number of transnational corporations based in developing countries has increased also. But those enterprises come from a relatively small number of countries and are concentrated primarily in extraction and mineral-processing industries or in low-wage manufacturing sectors. Only a few transnational corporations from developing countries have individually penetrated developed market economies to establish an internal investment position.

25. The sectoral composition of transnational corporations based in developed countries has expanded into several new areas. Technological change brought advances in micro computers, robotics, fiber optics, and ceramics which alter the structure of some industrial patterns, while near-horizon developments in such fields as genetic engineering and super-conductivity promise to create whole new sectors of productive endeavors. Thus far, these industrial activities are concentrated in the advanced developed countries, in terms both of innovation and initial production, with developing countries playing a minor role unless they offer significant internal market potential.

26. Technological developments also stimulate the very rapid transnational corporation growth occurring in service sectors. Many services are not tradeable in the traditional sense, and both customer demands and the regulated nature of many service industries require a direct investment presence if a foreign enterprise is to participate in a country's domestic service economy. While service enterprises are expanding rapidly, particularly in the financial, trade and information-processing areas, those service activities are being conducted also by industrial transnational corporations which choose to internalize these functions. Overall, services now account for over one half of the annual flow of foreign direct investment and roughly 40 per cent of the stock (of which nearly half is represented by service activities carried out by industrial enterprises). 18/ This growth in services ties together a wider range of business activities, broadening the integrative effect of transnational corporations while also deepening the penetration of international economic forces into national economies.

(b) The growth of non-equity investments

27. One of the elements most commonly associated in the past with the concept of foreign investment was the equity stake taken by a foreign investor in a local business enterprise. Equity position has been assumed to reflect the level of foreign control over operational decisions and the distribution of resulting business profits. Hence, equity issues are central to the historical struggle by developing countries to increase their participation in local transnational corporation operations as well as to transnational corporation concerns over risk assessment and expropriation/compensation standards that help safeguard or assure recovery of their initial capital investment.

28. The series of reports from the United Nations Centre, Transnational Corporations in World Development, outline a progressively expanding range of low equity and non-equity operations undertaken by transnational corporations that can include turnkey or supply and plant leasing operations, management contracts, co-production and co-marketing, contract or subcontract manufacturing, franchising, licensing, and a range of associated joint ventures. 19/ Low equity or non-equity ventures often respond to host country political desires, but they are driven at least as much by marketplace judgements. While minimizing a transnational corporation's immediate financial risk that its sunken investment can be taken by a host country, lower capital operations also recognize that transnational corporation competitive advantages now often lie less in the provision of equity capital and more in technological applications, managerial know-how, and international market access that may not require overseas equity capital investments. Non-equity arrangements based on these advantages can also enhance a transnational corporation's flexibility to respond to changing global conditions - a valuable characteristic in times of rapid change in both products and production processes.

29. The increase in non-equity ventures has several important implications for assessing transnational corporation operations and the need for international corporate standards. A preliminary conclusion is that this development could provide further evidence for the erosion of traditional dividing lines between trade, investment and monetary issues. Some non-equity transnational corporation ventures resemble transaction-based trade or financial operations that are short-term and have limited impact on a host country's development. In such non-equity arrangements, the transnational corporation does not establish a continued investor relationship, but rather seeks short-term benefits. The host country buyer has greater control and independence in decision-making but cannot be assured of a continuing relationship or follow-up dealings with the foreign corporation.

30. On the other hand, transnational corporations can enter into non-equity arrangements from a long-term perspective, investing resources into the venture or integrating it into the transnational corporation's global network as fully as if equity capital were involved. In these cases, the venture partners will negotiate shared control arrangements in relation to the value of their resource contributions but with assessments made from a perspective that incorporates the project's expected generation of benefits over its full life span. Thus, the key element for

assessing how non-equity ventures relate to transnational corporation issues is probably the level of transnational corporation commitment to a venture over the longer term - a notion that was captured both conceptually and functionally by equity ownership at an earlier period.

31. This conclusion has important implications for the discussion of such transnational corporation issues as ownership, control and benefit distribution standards. A trade-off seems inevitable between the degree to which a transnational corporation exercises control over a venture and its willingness to make a substantial commitment to the long-term viability and profitability of the venture, whether or not the enterprise involves a direct foreign equity position. The growth of low equity and non-equity ventures may also offer developing countries certain new channels to tie into global markets, either linked to transnational corporation partners or exploring for themselves the potential for non-equity participation in other economies.

(c) The spread of mixed-nationality corporations

32. Another important development for the transnational corporation code debate and questions of international regulation, more generally, is a change in the national identification of transnational corporations. The earlier perceptions of a transnational corporation were that of an enterprise headquartered in a single home country. This perception is consistent with the early demand of the United States-based transnational corporations for wholly owned foreign subsidiaries. While the largest transnational corporations often seem exempted from pressures for local ownership participation, the proliferation of competitive transnational corporations has expanded the number of enterprises willing to engage in joint venture operations across national borders, even on a minority ownership basis.

33. More recently, transnational business competition and technological developments have created cost and marketing pressures that force even the largest transnational corporations to adapt their organizational structure and management operations. These changes are reflected in the growth of intercorporate alliances, often between competing enterprises, that encompass a growing variety of transnational business arrangements, including the full range of non-equity ventures. While many of these arrangements were used in the past, their rapid expansion in key industries and importance to overall corporate strategy alter the nature and application of managerial control and reduce the relative importance of traditional equity-ownership-related measures.

34. Intercorporate arrangements among transnational corporations in the industrialized world reach across broad industrial sectors. Hundreds of joint ventures and collaboration arrangements exist in the oligopolistic automotive industry, where the nationality associated with famous corporate nameplates now bear little necessary relationship to the identity or location of the product's value-added activities. For example, an automobile model that recently made headlines as the hottest selling import in Japan is manufactured in the United States by a Japanese company that is itself nearly one quarter owned by a United States company. In telecommunications, a French/United States/Belgian telecommunications venture battled a United States/Dutch/Italian alliance over

increased sales in the Federal Republic of Germany market, while a major Japanese communications company placed its first overseas order for telecommunications equipment from the North Carolina facility of a Canadian firm.

35. Although this phenomenon is not widespread, the mixed national character of many transnational corporations provides an increasingly pluralistic backdrop for political discussions on international economic issues. Corporate executives attempt both to influence and outguess governmental readjustments to rule-of-origin definitions in light of "Europe 1992" proposals and the United States/Canada Free Trade Agreement. In debate over extending the voluntary restraint agreement that protects the United States steel industry, 34 members of California's congressional delegation support a bid for increased semi-finished steel imports deemed essential by California Steel Industries, "a major state business" jointly owned by Brazilian and Japanese steel companies whose imports come largely from related new extraction and production facilities in Brazil. ^{20/} Many United States corporations even view the development-oriented Generalized System of Preferences as critical to their competitiveness, arguing that excluding some newly industrializing countries would raise component import costs by tens of billions of dollars.

B. Impact of change on the United Nations code

1. Need for the code

36. Developments over the past two decades have enlarged the role of transnational corporations in the international system while in the process altering the transnational corporation universe. Both these impacts, and the interactive relationship between them, need to be assessed in relation to the rationale and prospects for a code on transnational corporations. Are past motivating factors still relevant; are code discussions in the United Nations directed at appropriate political and economic objectives; more specifically, are these entities, their activities and their impact important enough to warrant a framework; and are these activities sufficiently international that they require an international régime?

37. Transnational corporations are fast becoming the lynchpin for world economic activity, particularly in the most dynamic sectors of information-based technology and services. Transnational corporations act as a vehicle for organizing and integrating trade, investment and monetary transactions across national borders. Technological advances allow, and competitive pressures require, that enterprises "go global".

38. Although this change is by no means on a large scale, it has two important implications for the code debate's rationale. First, interdependent and integrating economic forces require an overview comprehensive enough to match the global span of transnational economic processes and impacts. Questions of international economic policy are now beginning to be treated more as a unified whole than in separated compartmentalized policy segments divided according to trade, investment and monetary issues. Transnational corporations, as the major organizational vehicle of this integration, are a central part of such policy considerations. This reinforces the need for an international framework that addresses the activities of these corporations.

39. Secondly, there is urgent need to address the emerging economic and geo-political pattern that threatens to split the world into two isolated economic blocs. Without conscious policy steps to encourage economic linkages between developed and developing countries, the large majority of the world's population will be consigned to a politically unstable and ethically unacceptable state of permanent "underdevelopment". Again transnational corporations, as the primary vehicle for functional economic integration, can play a constructive linking role, if guided within an appropriate international framework. To be fully effective, such a framework would have to address both governmental and private sector responsibilities in the international economic system, a principle that is already in the United Nations code.

40. Finally, many of the challenging new problems emerging in the international arena are truly transnational in character, both in terms of their impact and the manner in which they must be managed. An obvious example is protection of the environment, which is not divisible territorially since pollution of the air or oceans can quickly spread beyond political boundaries, requiring a co-operative international approach. Worker and product health, safety and quality standards raise other common international issues, especially since products and services are rapidly and widely dispersed through an increasingly interdependent transnational network.

41. While the control of potentially negative impacts is a concern, the facilitation of positive benefits is equally important. A supportive international framework is necessary for the continued liberalization of national foreign direct investment régimes, growth of global stock markets and securities exchanges, linked data processing services and media transmission facilities. Similarly, the protection of intellectual property rights, stability of component supply networks, and establishment of efficient and effective global marketing and franchising systems require compatible governmental approaches to regulatory goals and enforcement. These developments need co-ordinated definitions and regulatory processes that facilitate rather than impede business transactions.

2. Outstanding issues

42. In order for the code to fulfil all these important functions, the present impasse in the code negotiations will have to be broken. This might be possible by an application of political will that minimizes the debate over formulations of principles rooted in past controversies, focusing instead on the code's co-operative objectives, in the light of new geo-political developments and economic realities.

43. Among the concerns that stimulated the United Nations to undertake the code exercise in the early to mid 1970s were fears about potential transnational corporation interference in domestic political affairs, especially where corporations could draw on their home Government's political support, or indeed perhaps operated at that Government's behest as an arm of its foreign policy. Although developed countries are host to the vast majority of foreign direct investment, they generally feel less vulnerable to this type of outside pressure, so the issue was framed primarily in a North/South context.

44. In an applied sense, diffusing the political antagonisms surrounding transnational corporation issues has important implications for most of the unresolved issues in the United Nations code debate. For example, non-interference by transnational corporations in internal political affairs was a contentious topic early in the debate. Home Governments can now endorse the principle of non-interference without seeming thereby to accept allegations of widespread transnational corporation misconduct. In fact, the non-interference principle is now finally accepted by all sides in the code discussions, reducing this once burning political issue to a manageable debate over appropriate formulation.

45. The code discussions on the outstanding issues are often locked into a debate that no longer corresponds to the altered political and economic reality of transnational corporation operations. Innovative risk-sharing measures and conflict resolution procedures provide ways to manage problems associated with transnational corporation operations, but these practical changes have not yet carried over into the code discussions. The deadlocked debate over expropriation/compensation and a reference to international law or obligations is another excellent example in this respect. Even if the dramatic reduction of expropriation incidents during the 1980s may only be prima facie evidence of the decreasing importance of this controversy, more convincing are developments that appear to account for the declining expropriation figures, including both corporate techniques to reduce, manage or offset potential expropriation risks, and changing governmental practices that decrease the attractiveness or need for expropriation actions.

46. Corporations have increased their use of reduced and non-equity investments since the early 1970s, thereby decreasing their exposure to expropriation. Joint ventures, project finance, turnkey operations, and management contracting are among the techniques mentioned earlier that enable transnational corporations to share the burden of raising capital for new projects as well as spread the risk of subsequent losses. Additional progress is evident on bilateral and multilateral mechanisms to insure or otherwise guarantee against expropriation of investment capital.

47. Actions on the governmental side also push the significance of the expropriation/compensation debate further and further from meaningful reality. The historically central stake for developing countries in this issue was to reassert their permanent sovereignty over natural resources. National sovereignty is now an accepted fact, not an objective. Dealings with transnational corporations are pursued in the context of more equal bargaining over the market terms of a contract. Indeed, the initial emphasis on local ownership as the embodiment of national control over an investment is now a less important objective for many countries, which may aim instead at capturing a larger share of the economic benefits that derive from a transnational corporation's non-equity competitive advantages.

3. Application of the code objectives to contemporary transnational corporations

48. The broad objectives for a United Nations code of conduct on transnational corporations have been described as follows:

"The United Nations code of conduct on transnational corporations is meant to provide a stable, predictable and transparent framework that would facilitate the flow of resources across national boundaries and thereby enhance the role of foreign investments in economic and industrial growth. At the same time, the code is meant to minimize any negative effects associated with the activities of transnational corporations." 21/

49. This goal - to maximize the positive and minimize the negative - is still essentially valid and unobjectionable. Applying these objectives to the contemporary cast of transnational corporations, however, requires intensified efforts to match code concepts and transnational corporation structures. The types of transnational corporation changes outlined in the chapter above point to a rather qualitative mix incapsulated in the overall concept of a transnational corporation. The key to addressing the mixed range of contemporary transnational corporations with a code lies in stressing the code's functional approach, based on an understanding of their actions and impact. The fact that the code definitional criteria rely on operational factors more than equity characteristics constitutes an important built-in advantage.

50. The conceptualization of policies on transnational corporations within the code framework might therefore need to take into account these changes in a parallel fashion, to match the evolved and expanded group of enterprises that now crowd under the common umbrella label of "transnational corporation". In policy terms, these changes could mean that:

(a) The locus of effective responsibility for, or effective control over, many important international business operations is becoming more difficult to ascertain;

(b) A transnational corporation's overall commitment to a particular product line, stage of production, or geographical location is less stable over time, since less of a transnational corporation's own capital is directly invested and fewer business functions are internally integrated.

51. If these policies focus primarily on traditional transnational corporation types, or rely on the unilateral actions of national Governments, it will fail when applied to emerging international issues that arise from the growing range of interdependent business arrangements among transnational corporations from different countries. Thus, Governments might need to be prepared to adjust their responses in order effectively to address complex business structures and processes. This step does not require a redrafting of current definitions but the application of the code concepts to the types of transnational corporation-related issues that would need to be addressed currently and in the future.

52. It would be important, therefore, first to assess how the code concepts apply to issues affected by changing international business relationships that weaken central transnational corporation control mechanisms while dispersing both authority and responsibility. More transnational corporation activities are interlinked across national boundaries in ways that leave them not fully under the control of a single corporate office against whom national regulations can be applied. Attempts to apply national regulations to the full array of intercorporate partners in a global network would raise extra-territorial jurisdiction issues even more divisive than in the past. This change then places a higher premium than before on forging a broad international framework for managing such potential political difficulties. The objective should now be at least as important for home country Governments as for hosts, since formal control over the parent headquarters no longer guarantees effective control over the range of business dealings in which that transnational corporation may be involved.

53. A second major implication of this change relates to the notion of transnational corporation commitment and corporate responsibility. As transnational corporations emphasize non-equity investments and explore flexible arrangements among multiple business partners, a transnational corporation's long-term stake in any specific host location might be thereby reduced. A challenge for the code's follow-up discussions will be to account for this change in the consideration of ownership and control issues, while exploring ways to enhance transnational corporation stakes in the economic growth and social vitality of developing country regions, including business arrangements that can tie these areas more effectively into the global market system.

4. Emerging transnational corporation issues

54. An interactive dynamic exists, therefore, between changing transnational corporation characteristics and policy concerns associated with transnational corporation activities and influence. The policy issues raised by current transnational corporation operations may need to be assessed in order to determine how best to apply code standards to appropriate types of transnational corporation-related issues and to identify new concerns that may arise from evolving transnational corporation structures, functions, and sectoral concentrations. The essence of a code for transnational corporations revolves around identifying and addressing those issues that are particularly applicable to enterprises conducting transnational operations, even though the standards may also reflect good practice where relevant for local firms as well. Changes in macro-economic and geo-political factors, along with sectoral investment shifts and the metamorphosis of transnational corporation organizations, alter the mix of issues significant to transnational corporation discussions within the code framework. In some cases the application and outlook of traditional issues are transformed, while in other instances new or expanded topics arise to claim higher priority attention. A sampling of examples will indicate the possible impact of changing conditions on the context for future transnational corporation discussions and the possibilities they offer for renewed interest in the code.

55. New priority attention in the code's follow-up discussion might be due to matters such as the indirect employment impacts of transnational business networks, particularly their linkage function between developing and developed country markets. Transnational distribution and marketing operations can indirectly enhance employment objectives in developing countries by providing a channel for those countries' exports to the developed economies. Without ties to transnational corporation networks, preferably through long-term subcontracting or contracting commitments, the breadth and depth of these increasingly integrated markets may otherwise exceed the resources of most developing country exporters.

56. Cross-investments by transnational corporations located in the major developed markets reinforce interdependent ties between these regions, deepening both economic and political stakes in establishing co-operative multilateral relationships among governmental entities. Lacking a similarly balanced cross-investment position running north to south between developed and developing countries, the danger is that these regions will pull further apart. The challenge will be to encourage market linkage developments arising from the recent metamorphosis of transnational corporation structures in a way that supports North/South political as well as economic relations.

57. The role of transnational corporations in the international expansion of service sector industries is another development that raises new issues for the future transnational corporation discussions within the code framework. Service industries are among the most heavily regulated sectors within any national economy, providing fertile ground for international conflicts over the approach and application of national regulatory schemes. One reason for such extensive regulation of services is the extent to which these activities penetrate a country's economic and social fabric, touching the daily lives of individual citizens. Intangible flows of information, skills and financial resources, the assets upon which service sector competitiveness depends, cannot be kept as conceptually or practically segregated in a country's economy as the production of physical goods.

58. Service sector transnational corporations that introduce a "foreign" element into these domestic processes may thus raise a set of future political issues that are potentially more sensitive and challenging for international co-operation than traditional controversies over natural resource ownership or wage-rate exploitation. While transnational corporations provide the building blocks that allow for a dynamic and globally interdependent services network, a new level of international co-operation and co-ordination will be necessary to sustain the benefits of global integration in the face of nationalistic fears and pressures for restrictive unilateral regulation and control. Additionally, many provisions already agreed to in the draft text of the code are beneficial and directly relevant to discussions on trade in services and trade-related investment measures which are under way in the GATT-sponsored Uruguay Round of trade negotiations.

59. A possible extension of this activity would be to encourage further co-operation among transnational corporations and Governments in improving regulatory co-ordination in the international financial sector. In light of recent stock market events, co-operation appears especially imperative among the world's

nationally organized but functionally interdependent securities and commodities markets. International standards and co-ordination would help manage potentially destabilizing spillover effects while enhancing the efficiency and ensuring the integrity of market procedures. These efforts could lead to appropriate international standards of accounting, auditing and registration; promote better dissemination of information; and create international prohibitions against fraudulent conduct such as insider trading and market manipulation. Moreover, further steps might need to be taken to facilitate developing country access to established securities markets, while assisting in the mobilization of their own financial resources. These steps could lay the basis for the progressive incorporation of emerging markets into an internationally co-ordinated network that could exploit the efficiency of increased interdependence while minimizing the costs and risks involved in international financial transactions.

60. Recent efforts in the Uruguay Round of multilateral trade negotiations towards dismantling governmental measures that represent barriers to international trade, under the overall notion of trade-related investment measures and trade-related intellectual property measures, have also underscored the importance of certain restrictive business practices by transnational corporations, such as transfer pricing and restrictive business practices, as having potentially more distorting effects on international trade. The provisions of the code dealing with these issues could provide a basis for developing specific norms and procedures aimed at avoiding the negative effects of such practices.

61. Other business sectors offer similar opportunities to promote a framework that can sustain the further expansion of integrated world commerce, helping to bridge the gaps between economic regions. Many types of subcontracting arrangements can promote the beneficial integration of business across national boundaries, provided that the international community can co-operate to minimize unnecessarily restrictive governmental policies. Improved technology also now allows for communications systems that tie developing countries into transnational data processing networks, facilitating the transfer of information as well as providing improved job skills and opportunities.

62. The growth and interdependence of transnational business also creates a need for international attention to environmental and health issues that mutually affect business and governmental interests throughout the world. Similar international problems are now emerging in product-related health, safety, and quality standards due to the rapid increase and interdependence of world commerce. For example, in an integrated trading system, the incorporation of sub-standard counterfeit goods in manufactured products or residue pesticide levels in agricultural produce generate safety and reliability concerns among global consumers. Internationally agreed upon standards and procedures are necessary to avert difficulties that stem from the application of varying national criteria, laws, and regulations.

63. The safe and effective disposal of hazardous waste is another issue that is beginning to receive concerted world attention. The opportunity exists for co-operation between transnational corporations and Governments in planning for future storage and disposal needs, the prevention of accidents and/or leakages, and an overall reduction in hazardous waste products. Over recent years a number of

serious incidents involving toxic chemicals, radioactive material, and oil spills have forewarned the world community that risks from deficient environmental or safety standards fall not just locally but also regionally and even globally. A new initiative by the United Nations Centre on Transnational Corporations illustrates how the development of international guidelines and co-operative follow-up activities might be used in response to environmental issues. The Centre is exploring the formulation of criteria and principles that corporations could use in planning and managing their international operations, pursuing this exercise in a manner that addresses both public policy concerns and private business interests. Corresponding activities include determining the feasibility of a fund, financed by voluntary transnational corporation contributions, to support environmental preservation. Such efforts highlight the feasibility of a consolidated international framework, utilizing both private and public sector resources and input, from which to launch co-operative endeavors addressing global issues.

64. As with other issues that relate to the impact of international business developments, this new activity of the Centre points the way towards a code framework for co-operation among Governments, complemented by the active advice and assistance of transnational corporations, which could maximize recognized benefits of transnational business activities while preventing or minimizing potentially negative effects. The extent of the exercise's success, as well as potential progress on other new transnational corporation agenda issues, will depend in large measure on whether the general debate on the code can move from the past to the present. From this perspective, the code negotiations could look forward to a code that will be able to examine and encourage international discussion on emerging issues, rather than being relegated to mediating old disputes where participants are already locked into rigid ideological positions.

III. THE CODE OF CONDUCT AND THE URUGUAY ROUND

A. Interrelationships

65. It seems likely that the code will be successfully negotiated, despite previous difficulties. One reason for such a possibility is that many of the issues involved in the Uruguay Round of multinational trade negotiations have, in fact, been for years under negotiation in the code exercise, and some degree of consensus has been reached on them. The interweaving of trade and investment questions - so substantially demonstrated over the course of the past years - has been such that many of the features of a "level playing field" are in fact dealt with in the code negotiations. The Montreal Ministerial Declaration, for example, calls for further identification of the trade restrictive and distorting effects of investment measures that are or may be covered by existing articles of the General Agreement on Tariffs and Trade (GATT) and other investment measures that may not be covered adequately in existing GATT articles but are relevant to the mandate of the Group of Negotiators given by the Punta del Este Ministerial Declaration; the Group is also directed to consider development aspects that would require attention. 22/

66. Given the work of the Commission on Transnational Corporations, it would seem that these tasks could be advanced by consideration of the rather substantial achievements on investment measures which are contained in the current draft code. It may well be that the language of the articles so far more or less agreed in the code might be adjusted. But their relevance, and the relevance of the work done in achieving a rather substantial amount of consensus, to Uruguay Round objectives, is clear. Clauses having to do with national treatment, with balance between the interests of developing countries and of developed countries in investment matters, are surely fundamental to fair trade practice, especially in the light of present and increasingly growing internationalization of investment and of international investment as integral to world trade.

67. The code, even in its present incomplete form, might be useful to the elaboration of provisions regulating trade where, as in services, right of establishment is important. The code has the flavour of the environment in which it has been negotiated - that is, it reflects something of the concern of developing countries about unrestricted entry of foreign investment. The right to determine which investment may enter a country has traditionally been cherished as an inherent right of sovereignty. (This does not, of course, prevent that right from being bargained away to a greater or lesser extent - the right to make such a bargain being also an inherent aspect of sovereignty.) Developing countries have in the past worried greatly about control of their economies through foreign investment. That fear is not confined to developing countries alone. It is likely that, whether or not explicitly acknowledged in an understanding on trade in services, some aspects of the flavour of the code regarding right of entry will be reflected, whether by the listing of restricted industries, percentages of foreign investment, reporting requirements, or otherwise.

68. Thus, the provisions of the code on transnational corporations, and government conduct could, in many instances, be replicated in Uruguay Round conclusions. In this sense, the old concept of a "GATT for investment" - which, when proposed, seemed impractical to many observers mainly because fundamental principles had not been worked out or even openly debated - has now acquired a new vitality. This lends importance to ongoing discussions on the code and on the substance of its provisions, both in the context of the Commission on Transnational Corporations and in the debates centered on the Uruguay Round.

B. Trade in services and the code

69. The Uruguay Round of trade negotiations, now approaching its end, should thus produce renewed interest in the code, as well as in other efforts towards standards of conduct for, and treatment of, the foreign affiliates of transnational corporations. Code efforts have a considerable relevance, especially in the area (of great prominence in the Uruguay Round) of trade in services. 23/ Much foreign trade leads to foreign investment, in the natural evolution from "mere" trade to the establishment of operations in the country of destination of goods that are essential for the promotion of sales or the servicing of such goods. Where services are the "commodities" being traded, it is almost always necessary to have some sort of establishment (or investment) in the country in which such services

are consumed, it being the nature of services that they are produced and consumed in the country of destination. Since the topic here is "trade in services", there is a tendency to emphasize the trans-border aspects. But in most cases, in large industries, trade in services involves a foreign investment aspect. It also may involve immigration issues, as is, again, illustrated in the Canadian/United States Free Trade Agreement.

70. Where obstacles to trade in services exist, they generally take the form of regulation within the country of destination - not, as is more often the case with goods, at the border. In respect of trade in goods, most-favoured-nation treatment is the fundamental principle, with national treatment being important but in many respects secondary. The situation is different in respect of trade in services. In that situation, regulation is both internal and directed towards the supplier of the services. Regulations are directed towards branch banks, insurance companies, travel agencies, or the like - that is, towards entities established in the country of destination. Thus, the national treatment provisions of the several investment codes, whether they be the United Nations code, the OECD Declaration or even the bilateral agreements, such as bilateral investment treaties, become central to an understanding, within the Uruguay Round, on trade in services.

71. The OECD Declaration, for example, provides that Member States should, "consistent with their needs to protect their essential security interests and to fulfil commitments", accord national treatment to "foreign-controlled enterprises". 24/ The United Nations code, after stating the obvious right to control entry, goes on to provide fair and equitable treatment. This (despite the problem of defining exactly what constitutes such treatment) is an absolute standard, and, from the point of view of the trader-investor, a considerable advance on the purely comparative standard of national treatment (or, for that matter, most-favoured-nation treatment). In other words, even if the State in question acts unfairly towards its own investors, the provision requires fair treatment for the foreign investor. The United Nations draft code also includes the national treatment standard: "Subject to national requirements for maintaining public order ... entities of transnational corporations should be given treatment accorded to domestic enterprises in similar situations". 25/

72. In other respects relevant to trade in services standards, the United Nations draft code is arguably more apposite than the OECD Declaration and Guidelines. For a heavily regulated industry (as are most service industries) transparency with respect to governmental regulation is important. It is useful, for example, for a supplier of transport or communications services to know as much as possible about proposed new regulations and to be able to present a point of view in regard to such proposed regulations.

73. Transparency is in fact an important aspect of the OECD Guidelines; but the Guidelines are applicable to enterprises, not to States. They do not suggest that members (States) should open up the process of considering and issuing new regulations. In contrast, the United Nations draft code stresses "the importance of endeavouring to assure the clarity and stability of national policies, laws, regulations and established administrative practices". It also encourages the dissemination of "relevant information concerning decisions of competent

administrative bodies". 26/ There is of course great importance in publishing and making readily and widely available regulations which have been promulgated; the issue of the extent to which the process of arriving at such regulations should be "transparent" is a more complicated one, though it may be of equal, or, in some cases, greater importance.

74. These latter provisions are of more than slight importance to the service industries. Services, as noted, tend to be heavily surrounded by networks of regulatory standards, many of which are ambiguously phrased and often depend for their effect on obscure interpretations. Administrative decisions and interpretations are likely to be as - if not more - important, than the published regulations, in themselves often far from models of clarity. Publication of interpretations is not often a priority matter, and even finding the text of such interpretations is often difficult. The advances made by the draft United Nations code towards transparency are therefore not to be lightly discarded.

75. The useful provisions of the United Nations code should not be lost because of difficulty in reaching agreement on, for example, the standard of compensation upon nationalization. Investment disputes have been largely solved despite different theoretical preferences. The measure of compensation to be used in cases of expropriation has been found to be an issue capable of agreed compromise in many a settlement. Those are no longer matters that should frustrate agreement on the many rules of fair play which are present in the provisions of the code already accepted.

76. Moreover, the network of bilateral and multilateral agreements now in place and, even more, the intricate interlacing of economic interdependence which now exists argues that solutions will be found in the future probably more easily than in the past. These unsettled issues should not strip the international economic negotiations of the values found in a document like the United Nations code.

77. Finally, it is important that that code has been negotiated, over the course of all too many years, with the full participation of the developing countries. Concepts such as the Generalized System of Preferences and part IV of GATT do not amount to an international trade agreement that affirmatively contributes to their development. The area of services trade is one of remaining fields in which there is an opportunity to attain something like equality.

IV. PROSPECTS FOR AN EARLY CONCLUSION OF THE CODE

78. The growing significance of transnational corporations in the world economy increases the importance of concluding an international framework that would promote and guide essential functions performed by those corporations, particularly in mobilizing the capital, skills and technological resources required to meet world growth and development needs.

79. Global economic and political relations have changed over the past two decades, altering as well the manner in which transnational corporations conduct their operations. Increasingly interdependent movements of international trade,

investment and finance have restructured international economic relations. Government interests have evolved, influenced by the rate and pattern of economic development, regional interests, and emerging issues of common global concern. While ever more important, transnational corporations themselves also have changed. The cast of contemporary transnational corporations differs significantly from that of their predecessors in number and variety of sizes and countries of origin as well as in more qualitative aspects of operational control and managerial decision-making.

80. These changes reshape many of the determinative factors in the debate over transnational corporations. Original motivations and perceptions might no longer apply in the same way, particularly with the decline in political antagonisms over specific transnational corporation conduct. New and more systemic needs have arisen related to the evolving nature of transnational business and its impact on an increasingly integrated global economic network.

81. Newly evolving transnational arrangements appear to place a single nation's sovereignty more effectively at bay than did the unitary enterprises that existed when studies on transnational corporations first emerged. Elements of sovereignty are not being passed to some new international actor, however, but rather forfeited to a transnational economic process that needs a similar level of transnational policy response if public interests are to be served effectively. The draft code of conduct on transnational corporations provides the appropriate framework to deal effectively with new policy concerns and issues. Conceptually, the code reflects a dual structure, recognizing that the global economy operates through the collective interaction of Governments and the private sector. Follow-up actions under this code concept would seek a co-operative commitment to explore the means and methods for dealing with the political as well as economic dimensions of global transnational corporation issues.

82. As interests and issues change, the effectiveness of proposed responses calls for reassessment. But in order to address the challenges arising in the evolving international system, negotiations on the code of conduct must first be freed from early controversies; the validity of old disagreements need to be re-examined, and the direction for mutually beneficial new steps established. With a renewed political commitment, Governments can dismantle negotiating barriers that are now more symbol than substance, breaking the impasse that has held the United Nations code discussion for nearly a decade. Compromises are possible along the lines recently suggested by groups of experts.

83. A code agreement resulting from renewed efforts would mark a significant transition from conflict to co-operation. World development needs are too great and the potential contributions of transnational corporations too important to allow outdated antagonisms to block essential progress. Macro-economic trends and transnational business operations multiply integrative links between nations, but this development is neither evenly distributed nor irreversible. Without appropriate guidance from the international community, commercial processes may leave a backwater of underdevelopment that is politically and ethically unacceptable. Newly resurgent neo-mercantilism, whether manifested nationally or regionally, can threaten global ties, as can public policies based upon misconceived

or misapplied concepts regarding private enterprises. An international framework covering the conduct and impact of transnational business as well as government treatment of transnational corporations would help minimize friction and conflict while encouraging beneficial economic growth. The code would provide a stable multilateral framework and a platform from which to launch follow-up initiatives, combining public and private sector resources in pursuit of renewed growth and development.

84. Meanwhile, movement continues on co-operative, issue-specific agreements that address a range of international problems in a variety of multilateral forums. But unless a global comprehensive framework on foreign direct investment is adopted, more cohesive regional collections of countries will continue to deal with the issues that most concern them. The danger with this piecemeal approach is that it excludes some affected parties and ignores the ultimate political implications of such actions. If the world community possesses no vision of the future, activity will be defined by the pressures of the present, and those pressures are drawing nations into regional economic blocs that threaten increased political confrontations, especially along a North/South divide.

Notes

1/ The New Code Environment. Current Studies, Series A (United Nations publication, forthcoming).

2/ International Direct Investment: Global Trends and the U.S. Role. 1988 edit. (Washington, D.C., International Trade Administration, United States Department of Commerce, November 1988), p. 1; and Transnational Corporations in World Development: Trends and Prospects (United Nations publication, Sales No. E.88.II.A.7 and Corr.1).

3/ United States Department of Commerce, International Trade Administration Direct Investment Update: Trends in International Direct Investment. Staff Report (Washington, D.C., September 1989).

4/ Foreign Direct Investment, the Service Sector and International Banking. Current Studies, Series A, No. 7 (United Nations publication, Sales No. E.87.II.A.15), p. 5.

5/ United States Department of Commerce, Survey of Current Business (Washington, D.C., August 1989), p. 69. (Adjusted for the Netherlands Antilles' finance (except banking), insurance and real estate section.)

6/ "Recent developments related to transnational corporations and international economic relations: report of the Secretary General" (E/C.10/1989/2), 25 January 1989, pp. 14-18.

7/ International Direct Investment, op. cit., p. 77; and Amy Borrus, "Slowly but surely, the United States is buying into Japan", Business Week, (19 December 1988).

Notes (continued)

8/ For example, the Primary Dealers subtitle of the United States Omnibus Trade and Competitiveness Act of 1988 used reciprocity demands to force an opening of Japan's bond market to foreign firms. See also Monica Langley, "Trade bill conferees agree on limits for foreign dealers in U.S. securities" The Wall Street Journal (31 March 1988); and Michael Sesit and J. Terence Gallagher, "Japan unveils new measures to widen foreign role in government bond mart" (7 September 1988).

9/ Transnational Corporations . . . , op. cit., p. 57; and Raymond Vernon, "The product life cycle in a new international environment", in The Contemporary International Economy, John Adams, ed. (New York, St. Martins Press, 1985), pp. 408-422.

10/ Transnational Corporations . . . , op. cit., p. 80.

11/ The "convergence club" idea is adopted in application from the concept outlined in Technology and the American Economic Transition: Choices for the Future, Office of Technology Assessment, Congress of the United States (Washington, D.C., May 1988), p. 287.

12/ Transnational Corporations . . . , op. cit., pp. 33-40.

13/ Information provided by the Ministry of Finance, USSR.

14/ Ibid.

15/ Ibid.

16/ Information provided by the Foreign Investment Authority of Poland.

17/ "JVs, investments, Hungary-US Ties", Daily News (London) (27 June 1989).

18/ Ibid., p. 1; and Transnational Corporations . . . , op. cit., pp. 4-5.

19/ Transnational Corporations . . . , op. cit., pp. 67-71.

20/ "Congressional delegations battle over firm's attempt to raise steel imports", Inside U.S. Trade (9 June 1989), pp. 14-15.

21/ The United Nations Code of Conduct. Current Studies, Series A, No. 4 (United Nations publication, Sales No. E.86.II.A.15), p. 2.

22/ See "The Punta del Este Ministerial Declaration, part 11: negotiations on trade in services", GATT Focus (8 October 1986).

Notes (continued)

23/ For a detailed discussion on the relevance of the code provisions to the negotiations on an international régime on trade in services, see Key Concepts in International Investment Arrangements and Their Relevance to Negotiations on International Transactions in Services. Current Studies, Series A, No. 13 (United Nations publication, forthcoming).

24/ OECD, International Investment and Multinational Enterprises: Declaration by the Governments of the OECD Member Countries, 21 June 1976 (Paris, 1976).

25/ See proposed text of the draft code of conduct on transnational corporations (E/1988/39, Add.1, annex), para. 52.

26/ Ibid., para. 53.

Annex

REPORT ON THE HAGUE SYMPOSIUM ON THE UNITED NATIONS CODE OF
CONDUCT ON TRANSNATIONAL CORPORATIONS

15-16 SEPTEMBER 1989

Under the sponsorship of the International Law Association's Committee on the Legal Aspects of the New International Economic Order and of the United Nations Centre on Transnational Corporations, a group of prominent international lawyers from diverse national and juristic backgrounds participated in a symposium on the current status of the draft United Nations code of conduct on transnational corporations. The focus of attention was on the outstanding issues in the negotiations for the code of conduct, although the participants also addressed the need for such a code and the prospects for its finalization.

Need for the code

The participants endorsed the validity of the code exercise in the contemporary international economic environment. They felt that the code was still as critical as it had been at the inception of the negotiations some 13 years ago. Current international developments, such as the increased internationalization of economic activities, the phenomenal growth in the volume of trade and foreign direct investment flows, the emergence of services as an important component of foreign direct investment and trade, and indeed the entire phenomenon of increasing interdependence in the world economy, all underscored the importance of transnational corporations as major actors in the world economy. Those trends reinforced the need for an international framework for the operations of transnational corporations.

Outstanding issues

It was agreed that the outstanding issues in the code of conduct had important implications for international law, and the principal objective of the symposium was to invite distinguished and experienced international lawyers to review those issues, the divergent positions of the negotiating parties and the various formulations with a view to making an overall assessment as to whether the basic approach of the Commission on Transnational Corporations in the formulation of the various provisions was feasible or otherwise flawed on technical grounds. The outstanding issues in that regard were:

- (a) The question of a reference to international law/international obligations;
- (b) Non-interference in national political affairs;
- (c) Respect for national sovereignty;
- (d) Nationalization and compensation;

(e) Dispute settlement;

(f) National treatment.

The participants found no fundamental technical flaw in the basic approach of the Commission as to the outstanding issues. While some of the formulations could be refined or improved upon, the essential format of the provisions on the outstanding issues was considered feasible. If there was any impediment to the conclusion of the code, it derived from the lack of political commitment of the negotiating parties to the code and not the technical defects of the formulations. Conversely, flawless drafting could not by itself assure finalization of the code if the political will of the member countries was non-existent.

As to the specific outstanding issues, the general sense of the symposium was as follows:

1. The question of a reference to international law/international obligations

The importance of stipulating a reference to "international law" or "international obligations" in the code was underscored, although it was recognized that such a provision need not elaborate the substantive content of such law. After reviewing the debate on the doctrinal implications of referring to international law or international obligations, it was pointed out that for the purposes of the code, the distinction between international law and international obligations was not essential. That was because obligations of States with respect to foreign investment did not merely include obligations founded on conventional law but also obligations derived from customary international law. On the other hand, a State's obligations under international law must necessarily encompass its conventional as well as its customary legal obligations.

The discussion on the issue revolved around the text of paragraph 49 of the Chairman's draft, viz.:

"In all matters relating to the code, States shall fulfil, in good faith, their international obligations, including generally recognized and accepted international legal rules and principles."

It was suggested that the words "and accepted" in the context of that provision departed from the established phraseology in connection with the validity of international legal rules and principles, and should accordingly be deleted. It would be enough to retain the phrase "generally recognized" which had a clear technical connotation. With a further amendment, which was purely editorial, paragraph 49 should read as follows:

"In all matters relating to the code, States shall fulfil, in good faith, their international obligations, including those arising from generally recognised international legal rules and principles."

The amended text commanded general support, but other alternative formulations were suggested, namely:

"In all matters relating to the code States shall fulfil, in good faith, their obligations under international law."

and

"In all matters relating to the code, States shall fulfil, in good faith, their international obligations".

With regard to those formulations, it was pointed out that the terms "international obligations" or "obligations under international law" should not be construed as implying the internationalization of all obligations, such as obligations arising under contracts between States and transnational corporations.

2. Non-interference in internal political affairs

The importance of prohibiting transnational corporation interference in the national affairs of host States was acknowledged. A question was raised as to whether the concept of non-interference was feasible since it could imply severe limitations on normal business relations between a transnational corporation and its host State. However, it was the overwhelming sense of the symposium that the formulations of the code - namely, paragraphs 16 and 17 of the Chairman's draft - accommodated any legitimate corporate activities in the host State and were broad enough to encompass the divergent policies and practices of host countries in that regard.

The said paragraphs 16 and 17 read as follows:

"16. Transnational corporations shall not interfere in the internal affairs of host countries, without prejudice to their participation in activities that are permitted by the laws, regulations or established administrative practices of host countries."

"17. Transnational corporations shall not engage in activities of a political nature which are not permitted by the laws or established policies and administrative practices of the countries in which they operate."

It was felt that the above provisions captured the essence of the basic idea of the prohibition against corporate interference in internal political affairs and that it was impractical to itemize categories of prohibited activities. However, with regard to paragraph 16, it was suggested that the words "permissible under the laws" be substituted for the words "permitted by the laws", since activities which have not been expressly permitted may nevertheless be permissible because they have not been explicitly prohibited.

3. Respect for national sovereignty

The main issue which arose with respect of the discussion of paragraph 7 of the Chairman's text was whether the provision on permanent sovereignty over natural resources would be unequivocally qualified by a reference to international law. Since the basic approach of the Commission was to stipulate one omnibus provision on international law/obligations (para. 49), a clear linkage between paragraph 7 and paragraph 49 was recognized. The text of paragraph 7 (see below) was considered acceptable if read in conjunction with paragraph 49 on international law and also paragraph 6, which underscores the interrelated nature of all provisions of the code.

Paragraph 7 states:

"Transnational corporations shall respect the national sovereignty of the countries in which they operate and the right of each State to exercise its permanent sovereignty over its natural wealth and resources."

4. Nationalization and compensation

The sovereign right of a State to nationalize or expropriate the assets of a transnational corporation operating in its territory was recognized. It was also recognized that that must be coupled with a duty to pay compensation.

The participants felt that it was not feasible to spell out elaborate and specific principles on the standard of compensation, and that a general and flexible standard would be adequate, particularly in view of the provision on observance of international law/obligations (para. 49).

Accordingly, it was considered that paragraph 57 of the Chairman's text of 1988 was acceptable. That provision reads:

"It is acknowledged that States have the right to nationalize or expropriate the assets of a transnational corporation operating in their territory, and that appropriate compensation is to be paid by the State concerned, in accordance with the applicable legal rules and principles."

It was pointed out that the phrase "applicable legal rules and principles" embraced international as well as municipal legal rules and principles.

The point was made that the assets of a transnational corporation that may be nationalized or expropriated must be in the territory of the nationalizing State. However, that issue had been subject to different judicial decisions in different circumstances and need not be dealt with specifically in the code.

5. Dispute settlement

The basic principles set forth in paragraph 59 of the Chairman's text were found acceptable. Paragraph 59 provides:

"Disputes between States and entities of transnational corporations, which are not amicably settled between the parties, shall be submitted to competent national courts or authorities. Where the parties so agree, or have agreed, such disputes may be referred to other mutually acceptable dispute settlement procedures."

The first part of the provision provoked little comment. As to the second part, there was some concern as to whether the provision for referring disputes to "other mutually acceptable dispute settlement procedures" could not be construed so as to frustrate a prior agreement to submit to arbitration. That was because there was some question as to whether the second sentence of paragraph 49 envisaged two separate steps in the process - namely, an agreement to submit to arbitration and a subsequent agreement on the dispute settlement procedure or mechanism. It was pointed out that no two such steps were envisaged under the provision. It was understood that an agreement to submit to arbitration would cover both of those steps at the same time. Furthermore, the second sentence admitted of a choice of dispute settlement procedure either before or after a dispute arises.

Finally, the term "other dispute settlement procedures" clearly included international arbitration.

6. National treatment

The question was raised as to whether a provision on national treatment (para. 52 of the Chairman's text) was necessary in view of the agreement on paragraph 51 requiring "fair and equitable treatment" for transnational corporations, which is understood to imply non-discriminatory treatment.

However, if paragraph 52 were to be retained, it was suggested that it could be amended to read as follows:

"Subject to national requirements for maintaining public order and protecting national security and consistent with national constitutional law and basic laws, and without prejudice to measures specified in legislation and declared policies relating to the development objectives of developing countries, entities of transnational corporations should be entitled to treatment accorded to domestic enterprises in similar circumstances."

There was considerable debate as to whether it was necessary to provide for the possibility of preferential treatment of foreign investors, as stated in the last sentence of paragraph 52, which reads:

"Nothing in this paragraph should be construed as excluding the right of the host country to grant such special incentives and facilities to transnational corporations as may be considered necessary in its national interest."

The necessity of such a provision was questioned by some participants.