

**COMMUNICATION FROM CHINA, CUBA, INDIA, KENYA,  
PAKISTAN AND ZIMBABWE**

The following communication, dated 18 November 2002, has been received from the Permanent Mission of India on behalf of China, Cuba, India, Kenya, Pakistan and Zimbabwe.

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**INVESTORS' AND HOME GOVERNMENTS' OBLIGATIONS**

1. The annual flows of foreign direct investment (FDI) have risen sharply from US\$200 billion in 1990 to US\$1,271 billion in 2000 and have become an important channel of cross-border business activity. FDI flows can provide supplementary financial resources, technologies, managerial skills and employment opportunities and can play a positive role in the economic and social development of many host members, including the developing ones. FDI flows are generally undertaken by multinational enterprises (MNEs or in United Nations parlance transnational corporations - TNCs). MNEs have been characterized by their large scale of operations in many locations worldwide. They command enormous physical and financial resources, including proprietary technology and world-wide recognition of their brand or trade names. Their global scale of operations give them unique ability to respond to exchange rate movements in any part of the world, minimize their global tax bill and circumvent financial restrictions imposed by governments, ability to minimize the political risks, access to information on world markets and the ability to bargain with the potential host countries from a position of strength arising from their global position.

2. Given their massive economic power and their global operations, host governments have their limitations in regulating their conduct. In view of their objective of global profit maximization, there could be conflict of interests between their objectives and the development policy objectives of the host countries and they could indulge in restrictive business practices (RBPs), manipulation of transfer prices and other such practices. There is therefore a need to address the negative effects of the FDI activities by the MNEs that they may have on the host members, particularly the developing ones, while recognizing the positive role of the FDI.

3. In the 1970s there was a lot of discussion in international fora on the possible abuse of economic power by MNEs leading to appointment of an Eminent Persons Group by the United Nations in the early 1970s. The Group recognized the limitations of national regulations of host countries, particularly the developing ones, in regulating the activities of MNEs. Following the recommendations of the Eminent Persons Group, the United Nations Commission on Transnational Corporations was appointed. Among other steps taken, the Commission launched the negotiations on the United Nations Code of Conduct on TNCs. The negotiations on the formulation of the Code

began in 1977. The Code was to establish, among other objectives, the standards for the conduct of TNCs from all countries to protect the interests of host countries, strengthen their negotiating capacity and ensure conformity of their operations with (host country's) national development objectives. Substantial progress was made in evolving a Draft Code of Conduct on TNCs over the protracted negotiations. However, the Draft Code as evolved could not be adopted because of differences among the developed and developing countries on the legal status of the Code, among other issues, and was abandoned in 1992.

4. The limitations of national regulations in dealing with the operations of transnational corporations have been recognized in other international fora as well. For instance, the UN General Assembly Resolution 32/88 of December 1977 decided to convene a United Nations Conference on an International Code of Conduct on Transfer of Technology to be negotiated under the auspices of UNCTAD. The UNCTAD Code was aimed at providing general and equitable standards for international technology transactions. It also met the same fate as the TNCs Code. There have been other notable attempts to establish international codes relating to the behaviour and operations of TNCs. UNCTAD adopted the Set of Multilaterally Agreed Equitable Principles and Rules for the Control of Restrictive Business Practices in 1980. The International Labour Organization (ILO) adopted the Tripartite Declaration of Principles on Multinational Enterprises and Social Policy on 16 November 1977. Even the group of developed, and hence capital exporting, countries namely, the Organization for Economic Cooperation and Development (OECD) had been prompted to adopt in 1976 the OECD Guidelines on International Investment and Multinational Enterprises (subsequently revised in 1991 and 2000). The Working Group on Transnational Corporations of the UN Sub-Commission on Human Rights is currently discussing the responsibilities of TNCs to human rights, covering among other aspects, standards of consumer protection and employment practices.<sup>1</sup>

5. Although a number of steps have been taken by the international community to evolve codes of conduct of MNEs, all existing attempts have been of a voluntary nature. The developing countries had sought the UN Code of Conduct on TNCs to be a legally binding one. But that could not be adopted. As a result the growing internationalization of corporate activities since the 1990s has taken place without an effective global code that regulates the behaviour and operations on MNEs or to ensure corporate responsibility and accountability.

6. The glaring absence of an enforceable global code of corporate conduct has been highlighted by the recent spate of cases of corrupt corporate practices and fraud involving some of the biggest MNEs such as Enron, WorldCom. The bankruptcies of some of these corporations have affected investor confidence not only in the United States, where most of the companies concerned were based, but has also affected the global capital markets.

7. The series of financial crises in many developing countries in recent years have brought into sharp focus the speculative nature of financial markets and especially the operations of highly-leveraged investment funds, and their destabilizing and adverse effects on developing countries. For example, during the Asian financial crisis, criticisms were made of the lack of transparency of the workings of international currency markets, and proposals were made to make these markets and the highly-leveraged funds more transparent and accountable. However there has been very slow progress in the work in this area.

8. Therefore, legally enforceable norms of investors' or corporate conduct are urgently required to prevent such crises from reoccurring. They could also serve the useful purpose of protecting the global environment by prescribing the norms of corporate conduct with respect to environment, bring about transparency in the corporate dealings by prescribing the disclosure requirements and

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<sup>1</sup> See <http://www.unhchr.ch/html/menu2/2/sc.htm> for more details.

accounting practices, control restrictive business practices and curb the manipulation of transfer prices and thus improve global welfare.

9. The need for effective inter-governmental agreements and measures aimed at corporate responsibility and corporate accountability has been most recently recognized by the World Summit on Sustainable Development held in Johannesburg in August/September 2002. The Plan of Implementation adopted by the Summit states: "Actively promote corporate responsibility and accountability, based on the Rio Principles, including through the full development and effective implementation of inter-governmental agreements and measures, international initiatives and public-private partnerships, and appropriate national regulations, and support continuous improvement in corporate practices in all countries." The Working Group should therefore as a matter of priority take on the task of examining legally-binding measures aimed at ensuring corporate responsibility and accountability relating to foreign investors, including measures that clearly spell out investors' obligations and the obligations of their home governments.

10. The proponents of a multilateral framework on investment in the WTO have been seeking binding rights of foreign investors that the host member governments should agree to provide. However, not much discussion has taken place in the Working Group on what could be the obligations on the part of foreign investors or the home governments. The Doha Declaration indicates the need for balance between host- and home-member interests. It also underlines the need to take due account of development policies and objectives of host governments as well as their right to regulate in the public interest. Therefore, while recognizing the protection of legitimate rights and interest of the investing MNEs, the right of host members to regulate foreign investors and the need for foreign investors to undertake obligations in line with host members' interests, development policies and objectives, should be an indispensable part of the discussions in the Working Group. MNEs should strictly abide by all domestic laws and regulations in each and every aspect of the economic and social life of the host members in their investment and operational activities. Further, in order to ensure that the foreign investor meets its obligations to the host member, the cooperation of the home member's government is often necessary, as the latter can, and should, impose the necessary disciplines on the investors. The home member's government should therefore also undertake obligations, including to ensure that the investor's behaviour and practices are in line with and contribute to the interests, development policies and objectives of the host member. It is important that the Working Group addresses the issue of investors' and home governments' obligations in a balanced manner.

11. Some possible general principles that would need to be kept in view while drawing up any investor obligations could be as follows.

## **1. General principles**

12. These could cover the following broad principles:

- foreign investors would respect the national sovereignty of host member and the right of each member government to regulate and monitor their activities;
- non-interference in internal affairs of the host member and in its determination of its economic and other priorities;
- adherence to economic goals and development objectives, policies and priorities of host members, and working seriously towards making a positive contribution to the achievement of the host members' economic goals, developmental policies and objectives;

- adherence to socio-cultural objectives and values, and avoiding practices, products or services that may have detrimental effects.

## **2. Restrictive business practices**

13. There has been evidence on involvement of MNEs in anti-competitive arrangements with other firms such as horizontal international marketing and price-fixing cartels, vertical international distribution systems and restraints on parallel imports. It is argued that competition policy at the national or international level will take care of the anti-competitive practices. However, no multilateral framework on investment would be complete unless it covers provisions to deal with the RBPs associated with FDI.

14. In this context the provisions of the UNCTAD's Set of Multilaterally Agreed Principles on RBPs could be incorporated. These principles require that enterprises refrain from RBPs defined to include price fixing, collusive tendering, market or customer allocation arrangements, allocation of sales or production quota, concerted refusal to deal or supply to potential importers, collective denial to access to an arrangement. The MNEs are also required to refrain from abuse of market power in the form of predatory behaviour, discriminatory pricing or terms, joint ventures, M&As, and refusal to deal, among other provisions. Although the UNCTAD's Set exists, it is currently not a legally binding instrument and hence is not enforceable. Inclusion of its provisions into a legally binding investors' obligations with corresponding obligations on the part of home members to share information would help in their effective enforcement.

## **3. Technology transfer**

15. Technology is one of the most important resources that developing host members seek from FDI. Obligations of investors from developed members could aim to contribute to the strengthening of the scientific and technological capacities of developing members in general, and be required in particular to:

- contribute to technical and managerial training of citizens of host members;
- restrain from imposing restrictive clauses in technology transfer contracts with their affiliates and licensees that prevent absorption and assimilation of technology transferred.

16. As a pre-requisite for all members, especially the developing ones, to assess, select, develop and utilize technologies, international exchange on technical information and relevant guidance and training should be promoted and increased (especially concerning data on availability of substitute technologies). MNEs should provide data on various aspects of the technologies to be transferred, such as provisions of information needed for technical, institutional and financial assessment of the transactions, so that appropriate arrangement can be made in the host members to ensure that the technology transfer is meaningful and on most appropriate terms and so that inappropriate transfer or unnecessary turn-key transfers are avoided.

## **4. Balance of payments**

17. The operations of foreign enterprises are likely to affect the balance of payments of their host members in several ways *vis-à-vis* imports of equipment, raw materials, by exports of output and by remittances of dividends, royalty and other fees. Host member governments must be entitled to institute, as necessary, policies and measures to guard against the adverse effects on the balance of payments and to promote positive effects, resulting from foreign investment. This is to ensure that foreign investment contributes towards a healthy balance-of-payments situation, which is a major economic goal of the host member. Foreign investors should therefore be obliged to follow the

policies and contribute towards this goal. There is evidence suggesting that MNEs often impose trade-related restrictions on their affiliates that restrict the sources of their imports and affect their ability to export adversely. They are also known to transfer funds through manipulation of transfer prices. Furthermore, MNEs may also affect the balance-of-payments situation of host members with short-term financial borrowings or other financial transactions with their affiliates. There have been cases of MNEs applying their home governments' pressure to remit funds even though the host members may be facing extreme balance-of-payment difficulties thus perpetuating the liquidity problems. In light of this, there should be discussion on obligations on the investors, including to:

- adhere to policies and measures instituted by the host member governments aimed at safeguarding the balance-of-payments and at strengthening the balance-of-payments position;
- contribute to promotion and diversification of exports and to increased utilization of goods, services and other resources available locally;
- cooperate with the host governments in periods of balance-of-payments crisis by delaying remittances of profits and by phasing out divestment proceeds;
- desist from engaging in short-term financial operations or intra-corporate transfers in a manner that would increase currency instability and balance-of-payments difficulties
- apply fair pricing policies in intra-corporate trade and curb transfer pricing manipulations.

## **5. Ownership and control**

18. It is important that the MNEs give appropriate attention to the developmental needs of host countries through provisions of sufficient autonomy to their subsidiaries in the host members as well as to respect and adhere to policies of host countries relating to local ownership and participation. To be specific, among other things, the MNEs should:

- delegate as much as possible the power of decision making to their entities, so that the latter can contribute positively to the economic and social development of the host members;
- should work together with the governments and citizens of host members to realize the national objectives of local equity participation and effective exercise of control by local partners in accordance with contractual terms of equity or non-equity arrangements or with the terms of control as established by the laws of those members concerned;
- exercise their personnel policies in light of host member national policies, laws and regulations to the effect that priority is given to local nationals in recruitment, training and promotion to posts of managerial and leading nature so as to enhance the effective participation of local citizens in the process of decision-making.

## **6. Consumer protection and environmental protection**

19. There is evidence that MNEs often follow double standards with respect to consumer protection, environmental and employment practices in their home and host members. There have been cases that MNEs were selling products and medicines that were banned in their home members, were misinforming the consumers about their products (as in the case of baby food), adopting different environmental standards or norms of treating their employees. The Bhopal tragedy is typically illustrative in this context. A discussion on possible investor obligations may need to address the following:

MNEs should be required to:

- respect the rights of consumers in host members and pay due regard to effective consumer protection and ensure the safety and quality of the goods and services they provide and not to produce, market or advertise potentially harmful products;
- adhere to environmental and safety practices and requirements to ensure that the health, safety and environment of people in the host members are properly protected;
- take steps to protect the environment and to rehabilitate the environment when there is damage caused by the investor;
- respect the right of the host member population to know the names and types of dangerous chemicals used in the production process and size of their inventory, the undesirable effects resulting from their use and their accidental consumption and possible remedial measures to be taken in the event of an accident.

## **7. Disclosure and accounting**

20. The Working Group could also discuss the scope of investor obligations in terms of disclosure and accounting in relation to operations not only within the host member but with reference to all other transactions of the MNE which may impact in some way or another on host members' operations. This could include:

- acceptance to provide a disclosure on the financial as well as non-financial information on the structure, policies and activities of MNE as a whole, as well as that of the local affiliate;
- providing details of transactions with the affiliated parties such as parent or other group companies outside or inside the host member;
- transparency with regard to transactions in financial markets that have a speculative effect on the currency or financial markets of the host member.

## **8. Home governments' obligations**

21. The home governments' policies do have authority and influence over the behaviour of MNEs originating in their territories, in relation to the overseas operations of these MNEs. This authority and influence can be used in ways that have positive or adverse effects on the interests and development objectives of the host countries. Home governments should undertake obligations: (1) to refrain from policies or measures that influence MNEs originating in their territories to have operations or behaviour in host members that are adverse to the interests of the host members; (2) to institute measures that influence and oblige MNEs originating in their territories to behave and operate with full corporate responsibility and accountability in their operations in host members, and to fulfil their (MNEs') obligations to the host member and government, in accordance with the objectives and policies of the latter. As pointed out earlier, it should be recognized that in order to ensure that the foreign investor meets its obligations to the host member, the cooperation of the home member's government is often necessary, as the latter can and should impose the necessary disciplines on the investor. The home member's government should therefore also undertake obligations, including to ensure that the investor's behaviour and practices are in line with and contribute to the interests, development policies and objectives of the host member. The home member obligations should thus be an integral part of the Working Group's discussions. It is important that the Working Group examine obligations of the government of the home member of the MNEs, including the following:

- accepting obligations to enact legislation prohibiting foreign corrupt practices of their corporations and requiring them to follow in their overseas operations proper norms of consumer protection and environmental protection;
- undertaking to provide information regarding the involvement of MNEs in any questionable dealings and other information on their background that may be useful for the host government at the time of approval as well as subsequently;
- undertaking to cooperate with the host governments in control of RBPs, transfer-pricing manipulation, financial speculation and other unethical, irresponsible or unaccountable practices of MNEs, and in recovery of the liabilities of MNEs resulting from their mis-conduct in host members;
- undertaking to refrain from measures and policies that oblige or influence their corporations in their overseas activities to behave or operate in a manner that is detrimental to the interests of the host members;
- undertaking to institute measures and policies that oblige their corporations to meet their obligations to behave in a responsible and accountable manner in the host members, and that oblige their corporations to contribute to fulfilling the needs and development objectives of the host members;
- undertaking to refrain from policies and measures to restrict their MNEs on transfer or diffusion of technologies to their partners in the host members, including on the pretext of security reasons.

22. This paper has outlined some of the key issues that could usefully be discussed with respect to investors' and home government obligations in the light of the evidence on corporate behaviour and initiatives taken by the international community. The recent disclosures of corporate fraud and other malpractices have only underlined the need for greater disciplines on MNEs to bring about greater corporate responsibility and accountability. What is of serious concern to developing members is to ensure that the operations of foreign investors have positive effects and contribute to the meeting of national goals and development objectives of host member. Towards this end, governments of the host members must have sufficient regulatory powers and adequate policy space in relation to foreign investment, and the foreign investors should be obliged to respect the sovereign rights of host member states and contribute to their national and development objectives. Similarly, home member governments should undertake obligations to ensure the responsible behaviour of their corporations.

23. This paper is an initial reflection of views of the co-sponsors of this paper with regard to the issue of balance of interests between home and host members in the field of the relationship between trade and investment as emphasized in the Doha Ministerial Declaration, without prejudice to their right to further elaborate on all the relevant issues in this regard.

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