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Commission communication

I. Introduction

Economic developments in recent decades have been marked in particular by a very substantial growth of large undertakings which have industrial establishments distributed in a number of countries.

In most cases, the multinational growth of an undertaking satisfies the essential optimal operating requirements of natural economic and social conditions. It also satisfies, to a certain extent, the need to overcome the obstacles to the free interplay of international trade which States have still left in existence. The abolition of these obstacles would therefore eliminate a good many artificial reasons which lead undertakings to 'multinationalize' themselves without, however, properly satisfying real economic and social requirements.

In some cases such a movement can help to promote better distribution of work and knowledge throughout the world, to industrialize developing regions and to harmonize social conditions.

At Community level, as early as 1970, in its industrial policy memorandum, the Commission had already expressed regret that too many European industrial undertakings still retained a national dimension and were slow in adapting themselves, in size and location, to the new European economic area. The Commission found that the many legal and fiscal obstacles still in existence and the present lack of a European capital market serve to restrain this essential transformation of European industry. At the Paris Summit Conference the Heads of State and of Government wrote into their statement their wish to ensure that the Community had the industrial foundation on which its economic and social development depends. The Commission submitted to the Council an action programme capable of covering its initial phase.

With this in mind, the Commission considers that it should endeavour to remove the legal and fiscal obstacles hampering the transna-

tional integration of member countries' industrial structures, which should be able to develop by cooperation projects, by mergers of undertakings and even by the creation of multinational undertakings when they can make a useful contribution to attaining the Community's economic and social objectives.

Nevertheless, the growing hold of multinational undertakings on the economic, social and even political life of the countries in which they operate, gives rise to deep anxieties which are sufficiently divided, particularly in the areas of employment, competition, tax avoidance, disturbing capital movements and the economic independence of developing countries, to demand the attention of the public authorities.

The main reason for this is that these undertakings have reached a size and geographical spread such as to cast doubts on the effectiveness of the traditional measures of the public authorities and the trade unions, which up to now have been unable to achieve an equivalent degree of coherence or international integration. This situation has resulted in particular in inadequate national legal, fiscal, economic and monetary rules, the scope of which is too narrow to grasp the problems raised by the existence of numerous groups of companies legally separate and covered by different national laws.

In practice, problems begin to emerge as soon as an undertaking has production facilities in two or several countries. They obviously grow concurrently with the increase in the activities of the group of companies and their extension to a larger number of countries. Nevertheless the nature of the problems remains the same.

It should be pointed out that almost all the measures briefly analysed below are or will be carried out primarily in order to attain Community objectives which go beyond that of supervising the operations of multinational undertakings: this is particularly true of everything relating to the attainment of economic and monetary union of for example to tax-

ation or social policy. That is to say that virtually all the measures the Community might take with regard to multinational undertakings relate to problems which may equally well be created by national undertakings or even by private individuals.

The Commission therefore believes that it will be impossible to find solutions and allay anxieties in this area unless suitable counterweights are introduced at Community and international level so as to re-establish the conditions for a balance between the parties concerned.

By its very task, which is to coordinate, harmonize and if necessary supplement the policies of Member States whenever it is essential to seek common solutions, the Community presents the degree of effectiveness and cohesiveness necessary to form the framework into which such a counterweight can be introduced, even if still remaining imperfect: for this reason the Commission considers it useful to present the proposals described below to the Council.

Nevertheless, it is quite obvious that the activities of the Community will be fully effective only to the extent that identically inspired rules are imposed at world level with a view to ensuring a homogeneous framework for the operations of multinational undertakings whatever their origin and their geographic field of activity. The Community will work on this both in the appropriate international bodies such as the OECD and the United Nations, and, for certain points, within the framework of any bilateral negotiations.

The Commission realizes that the proposals described below do not solve all the problems. There are still some in the areas of foreign trade, the distribution of the results of research, the position reserved for foreign executives in management bodies, etc. for which the Commission has not at present been able to find a suitable reply. It is however necessary to undertake the implementation of measures which are feasible right away without waiting to find solutions to all the problems which emerge.

In this document, the Commission has therefore set aside the problems for which, for the moment, it has not been possible to define solutions. It should therefore be considered as the starting-point for measures which are about to be undertaken and subsequently finalized and not as an end result.

II. General guidelines for proposals

The Commission considers that the measures to be undertaken should not impede the development of a phenomenon with recognized economic and social advantages, but that they should merely aim at guarding the Community against its harmful effects with the help of a suitable legal framework. It also considers that this framework should contain no discriminatory aspect and that it should apply alike to individuals and to undertakings, whether of national, international, Community or extra-Community foundation.

The examination undertaken by the Commission indicated that the problems raised could not be solved by adopting a few spectacular measures or a code of good conduct which by definition would be binding only on undertakings of good will. Indeed, the size of certain problems, in particular relating to security of employment, tax avoidance or disturbing capital movements, justifies the adoption of measures of greater constraint.

Studies have moreover indicated that the range of possibilities which large international undertakings enjoy enables them to find an effective answer to meet specific isolated measures. The inevitable solution is therefore to set up a network of coherent measures ensuring for undertakings the degree of autonomy essential for the pursuit of their economic and social objectives, but sufficiently finely wrought to prohibit operations considered undesirable by the Community.

This had led the Commission to make an index of a certain number of measures, the implementation of which should help to solve

a large part of the problems raised. Some of these measures play a decisive role. Others are accompanying measures, each of which is essential only because it helps to ensure the cohesiveness of the system.

III. The measures envisaged

The various problems raised by the growth of multinational undertakings and the measures envisaged for solving them have been collected in seven chapters concerning:

- (i) protection of the general public
- (ii) protection of workers' interests
- (iii) maintenance of competition
- (iv) takeover methods
- (v) equality of conditions of reception
- (vi) protection of developing countries
- (vii) improvement of information

A. Protection of the general public

The gravity of the problems encountered in this area justify an active search for effective solutions. These problems in fact concern tax avoidance, security of supply, monetary stability, aid from public authorities and the protection of shareholders and of third parties.

(a) Tax problems

The area of taxation probably best reveals the inadequacy of nationally-devised systems supplemented by bilateral agreements for tackling the phenomenon of the growth of multinational undertakings.

The coexistence of different non-harmonized tax systems complicates and even often penalizes the international functioning of an undertaking. For this reason the Commission considered it necessary to submit to the Council two draft directives intended not to create tax burdens for operations carried out in several

member countries which are greater than for those carried out purely nationally.

Nevertheless, the very existence of disparities in tax systems has inevitably led multinational undertakings to attempt to protect themselves and even to use them in a way considered improper by some.

As regards legal tax avoidance, the Commission intends to follow up, as soon as possible, its work on tax avoidance, in order to improve international assistance and cooperation relating to information, supervision and recovery. Within the framework of this work, special attention will be devoted to the problems of transfer prices and licence fees. The possible adoption of certain tax agreements should, where appropriate, be envisaged in this context.

Moreover, the suggestions made by the Commission in the report on the taxation system of holding companies which it submitted to the Council in June this year also apply to multinational undertakings.

(b) Security of supply

In the event of a crisis, it is to be feared that the influence exercised by a non-member State which has jurisdiction over a multinational undertaking would be detrimental to the Community's interests.

In the sphere of energy, the Commission proposed to the Council measures intended to improve the Community's security of supply, in particular the concerting of action between the Member States and with the participation of the undertakings concerned on their hydrocarbons supply policy.

(c) Monetary problems

In this area the Commission considers that one of the principal measures should lead to a better knowledge of the financial flows accompanying companies' transnational operations.

It will therefore propose that a system of presentation of data concerning these flows be introduced at the external frontiers of the countries making up the Community.

The Commission has initiated the study of how to create better statistical information in order to show the influence of the multinational phenomenon on the balance of payments of the Community and of its Member States.

Moreover, a solution to the problem of short-term disturbing capital movements, part of which is attributed to the activities of multinational companies, is being sought, particularly within the framework of work on the achievement of economic and monetary union.

(d) The outbidding in aid by public authorities

In many cases, international investment plays an important part in the implementation of regional policies developed by public authorities.

Nevertheless, to the extent that Member States have recourse to a certain amount of outbidding in relation to State aid, particularly for regional purposes, in order to attract large new investment, multinational undertakings have been able to benefit more than others from this outbidding. Being among the first to decide on the location of their establishments, not in terms of such or such a national dimension, but in terms of all the possibilities provided in the geographical area of the Common Market, they could in fact place the different Member States in competition to obtain the greatest advantage for these establishments.

In order to eliminate negative effects, the Commission is continuing to develop its efforts as regards the coordination or harmonization of national, and particularly regional aids.

Moreover, in its stance on aid granted by Member States for a certain number of advanced technology sectors, the Commission has shown that it considered it was advantageous for the Community for European undertakings, confronted by the power of certain multina-

tional groups, to increase their efficiency, this increase involving in certain cases cooperation between these undertakings.

(e) Protection of shareholders and of third parties

In the near future the Commission will submit to the Council a proposed 'Law on groups of companies' which recognizes, on the legal plane, the subordination of the interests of particular companies to the group interests and which therefore legalizes the application of a uniform management policy for the group in relation to the companies forming part of it. Conditions as regards advertising are required to guarantee the transparency of the group. This draft also makes provision for arrangements intended to protect external shareholders. Creditors benefit from the guarantee of the parent company in the event of the failure of a subsidiary company.

B. Protection of workers

The opportunities possessed by multinational companies to affect employment in the various countries in which they exercise an activity causes much anxiety among workers. The Commission considers the setting up of a trade union counterweight as essential for a balanced solution to this problem; however that it is not its task to organize this but certainly to encourage it. The creation of Community joint committees or committees set up on a basis of parity by sector can contribute to this. Moreover, the Commission considers that the growth of European collective agreements can also help to solve the problems which the existence of multinational undertakings causes workers.

Adequate guarantees as regards security of employment may be furnished by the adoption of the following measures:

(a) The proposing of Directive on large scale dismissals

(b) The draft already in preparation aiming at the protection of employers' interests, in

particular as regards the maintenance of existing rights in the event of mergers or rationalization;

(c) The draft Directive on the harmonization of national laws on mergers between companies.

This last mentioned proposal includes specific rules for the informing and consultation of the employees prior to decisions by general assemblies, and for the negotiation of a 'Social plan' where the merger is likely adversely to affect employees' interests. In the event of disagreement, the public authorities may be asked by either of the parties to act as mediator. This Directive is concerned with mergers between companies in the same country, but the protective measures laid down therein must obviously also be respected in the case of an international merger, and the convention currently in preparation on mergers will have to contain similar provisions albeit merely for reference to national legislation.

In addition to the field of legal fusions, measures for the protection of employees should also be laid down in the case of acquisition of undertakings by other methods such as those provided for by the Dutch 'fusie code' (Merger Code).

It is also necessary:

(a) to adopt the European Company Statute which would ensure that employees of branches do actually participate in the supervising of the management of the parent company, and which provides for the possibility of concluding collective agreements between employees and administrative organs in the European Company.

Adoption of the fifth Directive would guarantee analogous rights at the level of the individual companies.

(b) Harmonization of labour law in order to guarantee real participation in the Works Council of the parent company for employees of companies which are members of a group.

In addition, the Commission is aware of the legal problem raised by the need for appropri-

ate representation of employees' interests vis-à-vis a company which no longer takes its decisions independently but complies with those of the group of which it forms part. In the course of the coordination of the law on groups of companies which it is at present undertaking, the Commission will examine the question as to what measures will have to be adopted in this field.

The provision of information for, and the participation of employees in cases where either the parent company or any of the member undertakings of the group are situated outside the Community raise substantial problems to which the Commission's departments are seeking adequate solutions.

C. *The maintenance of competition*

Most multinational undertakings are of considerable size and control substantial sections of markets. They are more able than other companies to restrict competition and to abuse dominant positions. It is therefore desirable in their case to devote special attention to ensuring that the rules on competition shall be respected.

This may be achieved by the following means:

(a) the adoption of the draft Regulation under Articles 87 and 235 establishing the incompatibility of merger operations making it possible to obstruct effective competition with the Common Market and laying down the obligation to give prior notice of merger operations involving undertakings or groups thereof with a turnover in excess of 1 000 000 000 units of account.

(b) active surveillance by the Commission in accordance with Articles 85 and 86 of oligopolistic situations.

D. *Purchasing of undertakings*

The increasingly frequent purchasing of competitor undertakings with or without the latter's

consent justifies the drawing up and application of a certain code of obligations concerning the ways in which such operations are to be carried out.

(a) it is desirable in the Commission's view to adopt Community rules concerning public take-over bids, and the preparation of such rules has been undertaken.

(b) the Commission is also of the opinion that a system for the rapid sharing of information and for coordination should be established as between the national authorities which supervise stock-exchange operations, in order that the latter may assess, on the basis of a complete knowledge of the facts, the often very extensive operations mounted simultaneously in several different countries by large companies. Such coordination ought in particular to allow a number of good conduct rules on stock-exchange operations to be drawn up and to ensure that these are respected.

(c) objective rules regarding the conditions to be satisfied by investment and take-over operations if these are to comply with the economic and social aims of the Community should be drawn up and applied by joint agreement by the Member States.

E. Equality of conditions of reception

According to the information available to the Commission, not all third countries are as liberal in the conditions which they grant to foreign companies as the Member States of the Community. The restrictions in question apply to the right of establishment, financing opportunities and conditions, the right of foreigners to hold capital in or directorships of companies, the sending-back of profits to the home country, or arise from the applications of national anti-trust provisions, etc.

At the present time various important changes are in cause. The disturbances in the interna-

tional monetary system, in particular changes in exchange rates, substantially affect the cost of investment as between the large economic groupings. At the same time, the attitude of trade unions in the United States might lead the American government to encourage foreign investment in that country. Finally, it has until now been and continues to be difficult to judge the possible consequences of Japan's new open policy with regard to foreign investments.

Under these conditions only a general approach can be outlined, detailed measures of which will have to be adopted at a later stage.

In any event the Community's aim in this field as in others is not to apply restrictive or discriminatory measures but to make liberalization measures more widespread.

In order to eliminate existing discriminatory situations as well as those which might arise from the unilateral application by the Community of the various measures described in this document, it will in the Commission's view be necessary:

(a) to hold meetings, and, if the necessary conditions here fulfilled, to negotiate on specific problems concerning above all the United States and Japan. During negotiations with certain countries the opportunity should be taken to tackle the problem of the tax facilities granted by these countries;

(b) to aim at the general adoption of most of the measures envisaged in this document throughout the industrialized countries, in other words as far as possible in the Member States of the OECD;

(c) to obtain guarantees in the specialized organizations of the UN (GATT, UNCTAD, UNID) to the effect that the provisions, which the Community may adopt unilaterally in order to ensure that the operations of multinational companies of Community origin shall correspond with the economic and social objectives of the developing countries, shall not operate to the latter's disadvantage.

F. Conditions of establishment of multinational companies in developing countries

A frequently substantial proportion of investment in developing countries is made by multinational undertakings. The economic and financial power of the latter may, in certain cases, result in substantial imbalances in the economic development of the developing country concerned, without necessarily being compatible with its long-term development aims.

The Community, particularly concerned as to the future of these countries, and desirous that an effective framework shall be created for balanced and mutually beneficial economic cooperation with them, will make every effort to ensure that investments by multinational undertakings of Community origin shall be closely compatible with the economic and social aims of the host countries.

Under this heading, the following measures, which would be especially effective, should be adopted:

- (a) The appropriate application of the economic and social provisions included in the proposals, concerning a system of guarantees for investments in third countries, which the Commission has submitted to the Council;
- (b) The objective application of Community rules concerning transfer prices and licence fees;
- (c) A development cooperation policy conceived in such a way as to encourage those private investments best suited to the priorities of the host country, and to govern within the framework of long-term agreements, the conditions of reception of such investments, and possibly detailed rules for implementation in cases of the transfer of ownership of industrial installations.

G. Better provision of information

In the Commission's view there exists a simple means of assuaging the fears felt in many quar-

ters and at the same time of throwing light on the operations of multinational undertakings.

This would amount to the most widespread possible distribution of an annual report containing straight-forward information on large national and multinational undertakings in order to allow all interested parties to arrive at their own judgement of the policies carried on by the various undertakings.

This information should, *inter alia*, include the following :

- (i) funds invested, re-invested, and transferred to the country of origin;
- (ii) the origin and composition of the capital;
- (iii) the number of jobs created and abolished;
- (iv) declared profits and taxes paid, as percentages of the turnover;
- (v) expenditure on research and income from licences.

The above would be broken down into the country where the parent company is established and all other branches of the group.

A substantial part of this information is already publicly available but is of relative interest in that it is not included in international comparative statistics, or else is not sufficiently compatible. The proposals at hand or in the course of preparation as regards company accounts and publicity should contribute towards attaining the necessary degree of clarity and compatibility, which at the present time continues to be lacking in some countries or in the case of certain types of company, the economic and social importance of which can no longer justify the degree of secrecy with which they surround themselves.

In order to be effective such action requires the support of the authorities in the Member States and in other States willing to cooperate, as well as the collaboration of multinational undertakings themselves.

IV. Conclusion

The mechanism constituted by the action set out above obviously cannot be established in one operation. Certain types of action already figure in formal proposals from the Commission which could rapidly be adopted by the Council. Others on the contrary will probably require many meetings of national experts in order to draw up the detailed rules required for their implementation. The process will take several years to complete.

In order to ensure coherent realization, according to the degree of priority accorded to each, of the types of action set out above, which fall within different Community policies, the Commission requests the Council to adopt the draft resolution in Annex I attached hereto, thus recording its agreement with the aims and principles expounded in this document, and its undertaking to participate actively in their implementation.

Draft Resolution of the Council

Draft Resolution of the Council on the measures to be taken by the Community in order to resolve the problems raised by the development of multinational undertakings

The Council of the European Communities

Having regard to the communication of November 1973 from the Commission on the problems raised by the development of multinational undertakings;

Whereas international economic interpretation may help to promote a more equitable distribution of labour and of technological knowledge in the world, and to harmonize social conditions;

Whereas nevertheless the size of the phenomenon gives rise to concern, in particular in the fields of employment, competition, tax evasion, disturbing movements of capital, the security of the supply of certain raw materials, and the economic independence of the developing countries; whereas the Community institutions must therefore take the necessary initiatives to ensure that multinational undertakings in their operations shall respect the economic and social aims of the Community;

Whereas the Community must participate fully in international discussions concerning certain problems of world-wide importance which would be begun within the framework of the various international organizations, for the seeking of resolutions in a spirit of reciprocity.

Whereas measures which may be adopted at the present time are concerned with problems which are not specific to multinational undertakings alone; whereas such measures fall in this different policies adopted or being developed by the Community in accordance with the Treaty of Rome;

(i) Confirms its intention to act within the time limits laid down in the various program-

mes in particular as regards the proposals concerning large-scale dismissals, protection of existing rights of employers in the case of merger or rationalization, the guaranteeing of investments in third countries, internal company mergers, the European Company Statute, the structure of S.E.'s and the supervision of mergers;

(ii) Considers that decisions have to be taken in particular in the fields set out above and notes the Commission's intention to submit as soon as possible proposals concerning the following:

(a) The protection of employees in the case of the take-over of companies;

(b) The laying down of Community rules in particular concerning stock exchange operations and on the origins of funds for investment.

(c) Cooperation between and amalgamation of national authorities responsible for the supervision of stock exchange operations;

(d) International assistance and cooperation measures in the fields of information, monitoring, and tax recovery, and in particular the drawing up of a joint schedule of transfer prices and licence fees;

(e) A body of law on groups of companies;

(f) The collection of adequate information on the international activity of undertakings.

**Analysis of the problems raised
by the development
of multinational undertakings**

I. Introduction

(1) No satisfactory definition of a multinational undertaking has yet been produced.

The simplest way is to define it as an undertaking with production facilities in at least two countries.¹ In that case, the concept of a multinational undertaking is practically synonymous with direct foreign investment and investment abroad.

Definitions which bring in additional, quantitative criteria (percentage of turnover outside the country of origin, number of countries in which the undertaking operates, etc.) are inevitably arbitrary. Definitions involving qualitative criteria (behaviour in the host country, nationality of its executives, strategy, etc.) are imprecise, because they are based on value judgements and produce complex classification systems of little practical value.

Consequently, two approaches are possible :

(a) Simply to list the names of undertakings that generally come to mind when concern is felt at this phenomenon (the multinational company), i.e., very large ones, which are foreign in relation to the person talking about them, and well entrenched in an oligopolistic and strategically important market.

(b) To take into consideration all direct foreign investment, 80% of which is certainly due to undertakings intuitively recognized by all as multinationals. Furthermore, the cumulative presence of foreign investments which are individually 'inoffensive' finally poses problems similar to those referred in (a).

Only the second approach makes it possible to use quantified data as a basis and will be employed generally hereafter.

(2) The reasons for locating plants etc., abroad are various:

(a) Labour costs: this factor operates only in the case of labour-intensive manufacturing industries. It is hardly operative at all today, except where the establishment of plants in developing countries is concerned.

(b) Protective barriers: these underlay the establishment of plants in Europe by multinational undertakings of many years standing, but are now a factor only in the case of semi-industrialized or developing countries.

(c) Transport costs: this factor will be of the first order only in the case of heavy products, which are generally of no more than limited interest to multinationals.

(d) Substantial penetration of an attractive market: this seems, indeed, to be the decisive factor as regards direct investments between industrialized countries. It is fairly clear that the opening of operations abroad will normally be done by a country or undertaking enjoying a lead in technology or competitiveness.

(e) Political factors may bring about a marked speeding-up in investment: the present wave of British investment in the Community is undoubtedly due to the U.K.'s joining the common market and the wave of Japanese investment that seems imminent is linked with the Japanese Government's present commercial and monetary policy.

(3) Sources of information on international investment are extremely deficient.

(a) Mandatory statistics specially designed to provide a picture of all aspects of the problem exist only in Canada.

(b) A certain number of countries keep a tally of direct foreign investment by monitoring capital flows requiring a foreign-exchange transaction. These data are neither full, nor accurate, nor yet consistent: while they often give a fairly faithful reflection of trends in investment movements, they give no idea of the cumulative size and the conduct of undertakings under foreign control.

¹ The entire range of economic activities covered by the term 'undertaking' (an economic entity) may be carried on within a single 'company' (a legal entity), but in this context will generally be carried on by a group of companies with links of control between them.

(c) In certain countries public or semi-public bodies carry out isolated or periodic surveys (the survey conducted by SORIS in Italy in 1965; the survey published in 1971 by the Belgian Office pour l'Accroissement de la Productivité; in the United Kingdom, the DTI's quarterly and annual surveys and the Steuer Report; annual surveys and 1966 census conducted by the US Department of Commerce; annual surveys in Japan; the survey conducted by the US Embassy in France) which provide a very useful supplement to purely financial statistics.

(d) At Community level, the Commission has put in hand several studies conducted on a very small scale (by the Institut Kienbaum for D.G. III, on the repercussions of a sample of ten investments; by the Institut Sorade, for D.G. I, on the influence of multinationals on the EEC's foreign trade).

II. Repercussions of foreign investment on the host country

(1) *The balance of payments*

It now seems to be accepted¹ that, in the medium term, direct investment abroad has a beneficial effect on the balance of payments of the investing country. Failing a large and continuous increase in foreign investment in a country, or financing carried out chiefly by capital imports² this investment will therefore generally have a neutral or adverse effect on the host country's balance of payments.

Generally speaking, it can be said :

- (a) that capital inflows and outflows for foreign investment and investment abroad do not exceed 3 - 4% of the total inward and outward flows in balance of payments;
- (b) that inflows and outflows between industrialized countries practically balance each other out.

(2) *External trade*

The foreign undertakings' share of the external trade of countries in which they have set up operations is now very substantial, and often exceeds their share of output.

Undertakings under foreign control provide 30% of Belgium's and 24% of the United Kingdom's exports of manufactured goods. Subsidiaries of foreign firms in Belgium export 65% of their output, in the Netherlands 55% (compared with 38% for Dutch undertakings).

Transactions between companies in the same group also account for a substantial proportion of external trade. Exports by subsidiaries of foreign firms to undertakings belonging to the same group, as a proportion of total exports of manufactured goods, stand at 33% in Canada and 10% in Belgium and the United Kingdom. Added to this, in the case of countries which are big investors, are exports by parent establishments to their subsidiaries, accounting for over 20% of US and 12% of British exports.

Subsidiaries of foreign undertakings generally have restrictions on their freedom to export. In the great majority of cases, the 'home' market (in their country of location) is reserved to them and they are barred from the parent company's market. The export-marketing area of foreign subsidiaries is, however, larger than is generally thought; in Belgium, for example, exports by subsidiaries of foreign, and especially American, firms are directed more towards non-Community countries than are those of Belgian undertakings.

¹ Recent studies by the Banque Jorjaan, the International Chamber of Commerce and the Department of Commerce.

² Between 65 and 85 % of the sums invested originate outside the investing country: the subsidiary's cash flow, Euro-bond issues, loans raised abroad. The export of capital for direct investment would generally be offset, in the balance of payments, by the income from the investment, after two to four years.

(3) *Financing*

According to the survey conducted in Belgium:

(a) The assets of foreign subsidiaries consist of 43% own capital resources and 57% outside capital.

(b) Investments by foreign subsidiaries are over 50 % financed:

- by self-financing, in half of all cases;
- in a quarter of all cases, by funds from the parent (these themselves, however, may be of various origins);
- in a quarter of all cases, by funds raised on the host country's capital market.

Cases in which the subsidiary itself goes to the capital market in its parent's country, or to the international market, are the exception.

The results of enquiries made about parent firms confirm the above orders of magnitude. In 1969, the financial resources of American-owned subsidiaries are believed to have originated as follows: 15 % from the USA; 26 % from non-US capital markets; 56 % from the subsidiaries' 'cash flows'.

In Japan, undertakings with a non-Japanese stake in them have an appreciably higher self-financing rate than Japanese firms.

(4) *Profitability and dividend policy*

The Belgian survey found that 71% of foreign undertakings were operating profitably, 27% showing a deficit and 2% breaking even. The loss-makers were chiefly in the textile and the nonferrous metals sectors, and were broken down comparably by country of origin. The average profitability of foreign undertakings, and particularly American ones, is higher than that of Belgian undertakings. A quarter of these undertakings pay dividends amounting to 58% of their profits (compared with 70% for Belgian undertakings quoted on the stock exchange). The corresponding figure for the United Kingdom is 56% (compared with 52%).

In Japan, the net profits and growth in turnover of partly foreign-owned undertakings are 50% higher than for wholly Japanese-owned undertakings.

In 1969, use of resources of US owned subsidiaries in the industrialized countries was as follows:

fixed assets: 57%

inventories: 17%

other assets: 11%

profits and dividends: 15%

Also worth noting is the fact that certain countries; the United Kingdom and the USA, for example, require of their undertakings — either by law or in practice — that subsidiaries repatriate their earnings.

(5) *Employment*

The proportion of industrial employment provided by foreign undertakings is 4% in France, 7% in the United Kingdom and 18% in Belgium. Between 1964 and 1968 foreign investment in Belgium created 70% of the jobs produced by new investment. Furthermore, 98 % of the net number of industrial jobs created by foreign undertakings in the period 1963-1968 (including those created by undertakings set up or taken over earlier) were due to undertakings set up by new investment, against 2% attributable to acquisitions.

(6) *Wages and industrial relations*

It would appear that gross hourly and monthly wages and salaries paid by foreign undertakings are on average slightly higher than those paid by indigenous ones. It has not been positively established that this difference still holds good when undertakings are compared on the basis of size category. Foreign undertakings would appear to have a greater tendency to link wage agreements with productivity.

Only in countries in which trade-union representation in the undertaking is not yet taken for granted may foreign firms have a tendency not to recognize the unions. In the United Kingdom it has emerged that foreign firms have fewer strikes than indigenous ones.

The 'hire and fire' labour policies, abrupt plant closures or mass redundancies, which foreign undertakings were often accused up to a few years ago of wishing to import into Europe, have certainly become rarer, or less sudden, in recent years.

(7) *Research and technology*

It is difficult to assess the technological impact of foreign investment, in view of the fact that it can take two forms, namely:

- the subsidiary's own, even independent, research activities;
- technology brought in from outside and assimilated by the subsidiary.

A British ad hoc survey failed to produce a conclusive answer to the question whether foreign investment have a favourable or unfavourable effect on the level of technology.

At all events, since the subsidiary is generally set up on the basis of the technological attainments of the parent, research activity is generally on a small scale and the technology balance is almost always in deficit.

In Japan, research expenditure by undertakings in which there is a foreign holding is less than half the Japanese average.

In Belgium, a quarter of the foreign subsidiaries have a research operation, with a certain degree of independence in half of these cases. It is noteworthy that the takeover of an undertaking does not seem to exert a preponderant influence on the level of research.

Half of the Belgian undertakings under foreign control pay know-how or licence fees to their parent company.

The Kienbaum Institut survey showed that there are some foreign subsidiaries with a sur-

plus on the balance of such fees. This is not at all typical, however, for in 1969, in West Germany, out of all undertakings with a substantial movement of fees and royalties, the balance was in surplus in the ratio 300:200 in the case of German firms, and in deficit in the ratio 5:500 where the undertakings were under foreign control.

(8) *Management*

In Belgium about half of the managerial staff (chairman of the board of directors, managing director, general manager, departmental managers) is of non-Belgian nationality.

This proportion varies (downwards) with:

- the length of time that the subsidiary has been established;
- geographical remoteness from the parent firm;
- the local stake in the subsidiary's capital;
- the job: 90 % of personnel and research managers are nationals, compared with only 60 % of general managers or controllers, and 40 % of managing directors.

Freedom in decision-making varies from the very slight, as regards capital spending, to very great in personnel and remuneration matters.

Foreign subsidiaries use more sophisticated management methods than indigenous undertakings:

- (a) firstly, because, as subsidiaries, their obligation to report back regularly and be under supervision dictates a more systematic approach to management;
- (b) secondly, because they often adopt more sophisticated techniques customary in the country of the parent company.

(9) *Behaviour in tax matters*

Taxation is one of the most contentious subjects concerning multinationals.

Even leaving aside any problems with tax evasion, it is undoubtedly true that domiciliation in various countries, each with its own methods and rates, and with independently conducted audits—each covering only half of a group's inter-company transactions—provides openings for tax avoidance. The prices charged in a group's inter-company transactions, and fees for industrial property or management, can be used as a means of reducing the tax assessment basis or of consistently moving profits to countries with favourable tax systems.

In the nature of things, there are no quantitative data available on this problem. Heads of multinational undertakings freely admit, however, that, if tax avoidance is not their *raison d'être* or their main source of profit, nevertheless they do logically operate a tax strategy that best serves the interests of their firm.

Merely by being true to themselves the multinationals thus come into conflict with the states, which consider that they suffer undue losses of tax revenue and see in this a challenge to their sovereignty, and with domestic undertakings which see in it a serious distortion of competition and one of the chief reasons for the rapid expansion of the multinationals.

(10) *The competitive situation*

Multinational firms are strongest in those sectors of industry in which oligopolistic concentration has gone furthest.

At least three quarters of foreign subsidiaries are branches of very large undertakings.

In Belgium, the foreign subsidiaries are appreciably larger than Belgian undertakings: whereas foreign subsidiaries account for 1.6% of the total number of firms, they make up 28.6% of those in the '1 000 workers or more' category. In Italy, joint-stock companies under foreign control are four times as large on average as domestic Italian companies. Although foreign holdings make up 20% of the capital of German companies, they account

for 47% in the case of undertakings with a capital of DM 100 million or more.

A total of 37% of foreign subsidiaries incorporated in Belgium have no competitors in that country, and another 19% have no competitors except Belgian subsidiaries of other foreign firms. Despite the extremely small sample used the Kienbaum survey identified similar trends.

(11) *Monetary aspects*

The situation here is very similar to that relating to taxation: a major impact on monetary speculation is often attributed to the multinationals. Whilst this impact may well be real, it is impossible to determine its extent.

Macro-economic studies carried out in the United Kingdom on items liable to speculative transfer did not detect any clearly abnormal movements in years of monetary upheaval as compared with 'normal' years.

Once, again, undertakings are acting perfectly normally in trying to provide against foreign-exchange losses, or even to make a profit, by moving their liquid assets about, or by means of leads and lags in payments between subsidiaries.

Nevertheless, without their having been a causative factor, since their speculative activities were additional to a monetary trend rather than *vice versa*, the possibilities open to the multinationals, which they do not deny using, have accentuated the speculative monetary movements of recent years.

(12) *Security of supply and manifestations of foreign sovereignty*

Apart from military hardware, no case can be quoted in which a country's supplies of a product have been adversely affected or threatened because they were provided by an undertaking under foreign control. Although obvious, this danger has been only a potential one so far.

The enforcement of US anti-trust laws on the US market, where both American and non-American undertakings are concerned, has more than once had major consequences for the structure and freedom of action of these undertakings in other parts of the world.

As the list of embargoed products has grown shorter, cases of orders being refused or cancelled by undertakings under foreign control have become less frequent. Nevertheless, the embargo still applies to subsidiaries of US undertakings and even to products embodying components of US origin.

(13) *Regional aspects*

In Europe foreign multinationals display greater flexibility as regards dispersal of locations, owing to their size, experience in this field and the fact that there is no traditionally predominant location.

They therefore site their establishments more often than do indigenous undertakings in recently industrialized regions (though seldom in under-developed ones which display structural disadvantages). A supply of labour of sufficient size and quality is generally the primary factor in selection, incentives being only a secondary consideration.

In the Belgian province of Limburg, where industrialization began in the very recent past, 58% of industrial jobs result from foreign investment.

Greater flexibility in choice of locations has as its logical corollary, however, an equal flexibility in disinvestment, either in the cessation or relocation of production.

III. **Repercussions on countries of origin**

(1) *The balance of payments*

As was said in II(1), investment abroad generally has a favourable effect on the balance of

payments, except during the period of initial amortization and, of course, unless the profits are moved to a country other than the country of origin.

(2) *Employment*

In the USA, in particular, the trade unions are mounting a very strong campaign against the setting-up of subsidiaries abroad by US firms. The chief reason for such investments, it is said, is the wish to evade US social organization and standards, its chief effect the substitution of manufacture abroad and imports to the USA for US exports: investing abroad is said to amount to the exporting of jobs.

Opposed to this view is another which states that this manufacturing activity and these jobs are created abroad only because exports can no longer be sustained owing to the dwindling of competitive advantages. The loss of jobs, it is said, would have been inevitable any way and is partially offset by investment abroad which generates orders for capital goods and semi-finished products.

Certain studies, whose objectivity is perhaps not beyond question, however, lend support to the latter view. According to ECAT¹, for example, American multinationals created state-side jobs in the period 1960-1970 at a rate 75 % higher than that of US manufacturing industry as a whole.

A recent study on ten multinationals, carried out for the US Department of Commerce, also reached the conclusion that investment abroad had the effect of reducing an unavoidable loss of jobs.

(3) *The trade balance*

By the same reasoning investment abroad has a favourable effect on the trade balance of the

¹ Emergency Committee for American Trade, a pressure group which aims to combat the trend towards protectionism and the limitation of investment abroad.

investing country. Imports to the USA of products manufactured abroad by subsidiaries of US companies were no more than 2.4 % of these firms' total sales in 1970 (9 % if US/Canadian trade is included, which since the agreement between the two countries on cars came into force, includes a very large proportion of American cars made in Canada). There has been practically no variation in this percentage since 1960.

Studies carried out hitherto have generally reached the conclusion that displacement effects (substitution of the subsidiary's output for exports of finished products) and entrainment effects (increased exports of capital goods or semi-finished products to the subsidiary) practically balance each other out, with a slight preponderance of displacement effects.

IV. The balance sheet

(1) It must be said first of all that the image of the multinationals in European host countries is tending to improve. Leaving aside the public-relations effort, this is probably due to:

(a) a better understanding of the facts, resulting in the recognition both of the beneficial aspects and of the irreversible nature of the phenomenon;

(b) the disquiet or opposition aroused in investing countries, which has had the feedback effect of putting the phenomenon in a better light in host countries;

(c) the fact that multinationals have made great progress in adjusting their behaviour and management to the social and cultural environments in which they set up subsidiaries;

(d) the fact that an increasing number of countries, after being host countries only, are now in their turn investing abroad, so that the multinational-company phenomenon is beginning to appear less one-sided.

The foregoing must be accompanied, however, by important riders and qualifications. It is

almost always true with regard to the individual firm or at local level, where the effects on employment are most apparent. The Kienbaum Institut's survey, for example, established that the attitudes of the local authorities, business organizations and trade unions are—practically without exception—either neutral or favourable.

The attitudes of those who take an overall view, however, are much more guarded.

Furthermore, the statement (i.e., that the multinationals' image is tending to improve) can be made only in respect of relations between industrialized countries. In the developing and semi-industrialized countries, mistrustful attitudes and control policies are becoming general.

(2) Analysis of the repercussions of foreign investment and the multinational company phenomenon brings out the fact that they are unfavourable in very few cases, but that foreign investments can give rise to apprehension of two kinds.

The first kind concerns the prejudicial consequences that might, for countries with a heavy concentration of undertakings under foreign control, spring from certain potential forms of conduct by the latter. These consequences (e.g., in the fields of employment or research, or relating to regional policy, or monetary matters, or security of supply) are not such that they can be definitely linked with individual undertakings, but would be the cumulative effects of the multinationals' conduct. They are therefore difficult to cater for by means of rules or action having effect at a specific point.

Secondly, there are situations in which the conduct of one undertaking, in isolation, arouses unfavourable reactions, even if its macro-economic impact is negligible. This occurs chiefly with regard to tax matters and competitive positions.

(3) Annex II pages 26 to 28 reviews the types of regulation governing foreign investment in force in industrialized countries.

Imbalance in this sphere may result either when attitudes to foreign undertakings differ widely between countries, or more especially when a country which is both host country and country of origin puts investment in its own territory at an appreciable disadvantage as compared with its own investments elsewhere.

It is often said that the non-US investor encounters numerous difficulties in setting up in the USA, and that US regulations are substantially more stringent with regard to European investment than are European regulations with regard to US investment.

If this were so, imbalance would exist, since US measures for the restriction of the export of capital are hardly any stricter than those in force, for example, in France and the United Kingdom.

On examination, however, it is apparent that the chief obstacle to foreign investment in the USA is in the toughness of competition on the US market. Non-US firms enjoying the minimum competitive lead to enable them to set up successfully on the US market are still a minority.

The level of competition also explains the independent mode of conduct which foreign subsidiaries operating in the USA readily adopt towards their parent establishments: once having successfully established themselves on that market, they very soon take the view that they have nothing to learn from those who are not acquainted with it.

Financing problems also have less to do with discriminatory regulations than with the lack of confidence of US bankers in non-US firms. And, unlike the conditions experienced by US investors in Europe, this is not sufficiently compensated for by the presence of foreign banks in the USA.

Other difficulties, e.g., the strictness of the anti-trust laws, are real but not discriminatory since they are enforced just as stringently upon US undertakings themselves.

Two objective obstacles do exist, however, and they certainly have discriminatory or restrictive effects.

(a) The Interest Equalization Tax penalizes the buying of non-US securities by US citizens, the aim being to limit the export of capital. This tax also penalizes issues of securities by European companies wishing to finance investment in the USA on the American capital market.

A subsidiary incorporated in the USA is not affected by this tax but generally cannot provide the necessary guarantees.

It appears, however, that the US Government intends to abolish the IET, or to exempt funds intended for investment in the USA from it.

(b) The citizenship requirements for shareholders and management personnel which undertakings must meet if they are to be defence contractors can greatly reduce outlets in certain sectors.

As regards Japan, which hitherto could hardly be accused of operating a one-sided policy, since its direct investments in industrialized countries were minimal, the coming months will show whether it follows through the investment movement which it seems to have initiated, and whether it will confirm its formal removal of restrictions on foreign investment in Japan by a truly neutral policy.

(4) While direct foreign investments enjoy increasing acceptance by the public and are almost always sought after by governments, this applies only to new ventures.

Takeovers of existing firms can also be beneficial, inasmuch as they save firms from liquidation, or improve their competitiveness by an injection of capital, technology and management.

Nevertheless, the beneficial results are much less tangible, and public opinion and governments find it much harder to accept them, especially when they are achieved against the will of the management of the acquired firm or are the work of powerful conglomerates.

(5) Summarizing, it can be said that the concern aroused by multinationals is difficult to relate specifically to particular forms of conduct or to clearly identified firms, but rather arises out of the imbalances induced or shown up by the advent and growth of the multinationals. These imbalances have given rise to feelings of frustration and disquiet which are no less real for being based chiefly on potential dangers.

Firstly, the advent of multinational undertakings has upset the interrelation of forces between the three traditional parties to discussion: firms, unions and governments. The latter two often find themselves in discussion with multinational undertakings of a size out of proportion to their own, whose decision-making centre is located outside their area of activity, and with whose capabilities and full configuration they are poorly, if at all, acquainted. Industry has built up a lead in the process of internationalization which the trade unions and States do not seem likely to shorten at present, despite their endeavours to cooperate and integrate.

Secondly, there is a manifest imbalance between those countries—even industrialized ones—which seem fated to be host countries and those which are big investors. The 'American challenge' or 'neocolonialism' attitude, together with apprehension regarding employment, security of supply and economic sovereignty, is found chiefly in countries with a marked deficit in their 'investment balance'.

Countries—even ones relatively modest in size like Sweden or the Netherlands—which themselves have large multinational undertakings have far fewer complexes of this kind, despite the fact that a combination of foreign and indigenous multinationals does nothing to make a government's task easier.

Lastly, multinational firms are a phenomenon that has accentuated the existing imbalance between large and economically powerful countries and the rest. The USA, for example, has sufficient scope for action to enable it to

exercise a certain degree of control over the conduct not only of its own multinationals but also of those of non-US origin, on the US market and sometimes elsewhere. This undoubtedly intensifies the feeling of frustration of countries which are mainly host countries.

Some details on the size of this phenomenon

(1) The actual value of industrial assets under foreign control throughout the world may be estimated in 1972 at \$ 240 000 million,¹ two-thirds of which are in industrialized countries. The corresponding turnover may be assessed at \$ 320 000 million, i.e. equal in size to world trade.

(2) The proportion of foreign investments in the economy of the Community countries is somewhere in the region of 15 %: approximately 9 % in Great Britain,² 10 % in France,² 14 % in Italy,³ 15 % in the Netherlands,² 18 % in the Federal Republic of Germany,³ 33 % in Belgium.² On average, two-thirds of the investments are from countries outside the Community.

(3) It is widely known that foreign interests occupy an important, and sometimes even predominant, place in several major sectors of Community industry, such as computers, hydrocarbons, the food industry, plastics, electrical engineering, the car industry.

(4) Among the countries which invest on a large scale, the most prominent are the USA, the United Kingdom, Switzerland, Sweden and the Netherlands.

Although the relative predominance of the USA is on the decline, the absolute value of its foreign investments is still increasing. It still accounts for 60 % of the world's total foreign investments, and between 40 % and 50 % of foreign investments in the Community countries.

(5) The balance of direct investments as between the USA and the EEC is approximately 4/1, the Netherlands being the only member country with a positive balance.

(6) The ratio of new installations to takeover of existing firms is approximately 7/3 in Bel-

gium and Great Britain, and 9/2 in the Federal Republic of Germany.

In Belgium, the percentage of takeover is much higher where the investments by certain European countries are concerned. They are particularly frequent in the food (50 %), wood and paper (38 %) and non-metallic minerals (38 %) sectors.

Approximately 5 % of foreign industrial establishments are branches without legal personality.

The level of foreign participation in subsidiaries is about 80 % in Belgium, the United Kingdom (90 % in the case of US subsidiaries) and the Federal Republic of Germany.

(7) It is not really possible either to confirm or to refute the forecasts according to which the world economy is becoming concentrated in the hands of a few tens or hundreds of multinationals. The growth in investments, turnovers and takeovers is certainly spectacular. Yet the rates of concentration are not increasing at the same pace, owing to the simultaneous expansion of uninationals and the birth of new firms.

At the same time, with more and more undertakings becoming multinational, the trend is towards an increasing number of multinational companies.

¹ By applying to the latest known book values an annual growth rate of 10 %, a book value/actual value ratio of 100/150 and an owned assets/controlled assets ratio of 100/15.

² As a percentage of the turnover or sales of the manufacturing industry.

³ As a percentage of companies' share capital.

National policies

A. with regard to foreign investments

(1) All non-Communist countries except Japan encourage, at least at the regional or local, if not the national level, foreign investments which create employment.

(2) a. A large number of member countries of the OECD place restrictions on foreign investments, using various methods:

— the banning or limiting of foreign interests in certain sectors: Canada, Finland, United States, Japan, Sweden, Australia, Norway, Spain;

— the prohibition or any investment from certain countries: United States;

— government authorization or control of foreign investment: France, United Kingdom, Japan, Norway, Finland, Sweden, Spain, Australia;

— special regulations governing undertakings under foreign control: Portugal, Switzerland, United Kingdom, United States;

— the exclusion of foreign-controlled undertakings from certain benefits or certain markets: Canada, United States.

It should also be noted that certain regulations which are in principle non-discriminatory, such as regulations on mergers or takeover bids, may be used to stop foreign investments. In the same way, political decisions having no legal basis have proved equally effective.

b. Within the Community, France has regulations requiring authorization for extra-Community investments.

Belgium has made it necessary for foreign takeover bids to be authorized and for the acquisition of major holdings to be notified. The United Kingdom exercises control over foreign investments by means of foreign exchange control and by laws on competition.

In certain cases, Member Governments have imposed a veto or laid down conditions on purely political grounds.

c. A European undertaking which wants to set up on the United States market faces numerous difficulties. Some of these take the form of discriminatory treatment found in a number of countries:

— foreign investments are prohibited in certain sectors: mining concessions, radiocommunications, shipping under the United States flag. Licences for the atomic energy sector may be granted only to United States firms and citizens;

— it can be very difficult to obtain work permits for non-United States personnel;

— the Buy American Act penalizes imported goods, thus making it hard for an overseas firm to gain the necessary market experience before deciding where to site a new production plant; moreover, in certain States, it also affects goods produced by foreign subsidiaries in the USA, and this also applies to defence procurement.

The difficulties created by regulations relate to financial regulations and anti-trust legislation:

— United States banks proposing to finance foreign groups have to obey very strict rules;

— foreign undertakings are not authorized to make share issues of less than \$ 300 000;

— share issues, acquisitions of holdings, takeover bids and share exchanges are made subject by the Securities and Exchange Commission to extremely meticulous formalities (this is true even in the case of the transfer of a holding in a US undertaking from one foreign undertaking to another outside the United States);

— the biggest obstacle in this sphere is the Interest Equalization Tax which consists of a tax on any United States purchase of bonds or shares issued by a foreign firm and which therefore handicaps foreign undertakings wanting to be financed on the United States market.

The problems of financing caused by these regulations (combined with the very high competitive level in the United States, which is by far the main obstacle to direct foreign investment in the USA) often make it more worthwhile for the foreign undertaking to establish itself on the United States market through a takeover or a joint subsidiary. This, however, involves the danger of anti-trust proceedings, especially in the case of large undertakings, and it is a threat which may materialize years after the new firm has been set up.

B. *with regard to investments abroad*

(1) Policies for restricting, controlling or directing investments abroad are generally linked with balance of payments difficulties. They usually involve foreign exchange control. This has been the case in many industrialized countries in the post-war years.

Whereas Japan has recently liberalized investments abroad, France, the United Kingdom and Sweden, for example, still have control measures, but apply very liberal policies.

Since 1960 the USA has introduced a number of measures, without including exchange control, in order to reduce exports of capital. Since 1968, acquisitions of holdings of more than 10 % in a foreign firm have been subject to authorization.

(2) With regard to support for investments abroad, most of the countries belonging to the OECD encourage investment in the developing countries by means of a government guarantee on investment and occasionally by providing capital.

As to investments in industrialized countries, the USA supported them in the immediate post-war years. For differing lengths of time, Germany, France, and Japan have had a favourable attitude towards investments abroad without, however, adopting any measures of support.