Achieving a Balance in the Rights / Obligations of Companies and Countries

Abstract

This paper reviews the state-of-play with international investment agreements, particularly focusing on the distinct levels at which they operate, and on the shifting policy pendulum between forces for liberalization and for regulation, since investment rules started being discussed in the 1940s.

The first contribution of this paper lies in the discussion of new issues for inclusion in international investment agreements, in order to achieve a more balanced approach towards the rights and obligations of firms and countries. Reviewing options for progress in improving the rights of countries (especially developing countries), it is concluded that there are only limited possibilities within the WTO itself since country-specific measures are required. An argument is presented for supporting voluntarism alongside regulation, with initiatives from both MNEs (through corporate social responsibility) and host countries having some merit.

1. INTRODUCTION

The history of international investment agreement (IIAs) has seen radical shifts in the public policy pendulum as represented by the balance of forces for regulation as compared with liberalization (Brewer and Young, 2001). In the recent past, liberalization forces have predominated, leading to strong bargaining power for multinational firms (MNEs) in their relationships with host governments - in all countries but especially those in the developing world. Since the final years of the last millennium, a new wave has begun to emerge, putting back on the agenda the issue of the obligations of companies and the rights of the countries (and communities) in which they operate.

The objective of this paper is to review these developments and discuss options for progress both within and outwith the World Trade Organization (WTO), where the aim is to improve the development prospects of poor countries. Within the continued liberalization framework existing currently in the global economy, the continued flow of foreign direct investment (FDI) by MNEs has a crucial role to play. However, this paper proposes that the MNEs' role should be expanded to encompass wider economic and social responsibilities if the forces of anti-globalization and protectionism are to be forestalled.

The remainder of this paper is structured as follows. Section 2 will provide a brief background of the current state-of-play in terms of international investment regulation, characterizing the evolution at the multilateral level, and the current patchwork regarding international investment agreements. The third section will address the 'shifting policy pendulum' between forces for liberalization and regulation and, using economic and bargaining power arguments, will analyze how we got to where we are. Section 4 will focus on new issues for inclusion in order to balance rights and obligations of companies / countries, many of which are sensitive and not within the

remit of the WTO, or of a multilateral investment agreement, hence increasing the complexity and making a consensus more difficult to reach. Section 5 will debate options for progress. The final part presents some concluding remarks.

2. STATE-OF-PLAY WITH INTERNATIONAL INVESTMENT AGREEMENTS (IIAS)

International investment regulation is an area prone to considerable controversy. In particular, an agreement on multilateral investment rules has not been reached and it does not seem likely to be accomplished in the near future (Young and Tavares, 2004). The issue has been debated since the 1940s, when the Havana Charter that would have created the International Trade Organization was rejected by the US Congress. FDI-related provisions were included, and were among the least consensual. Since then, and as Brewer and Young (2000) put it, the history of multilateral investment rules is a tale of successive disappointments.

After that big blow in the 1940s, FDI was vastly neglected in the agenda of multilateral institutions - especially of the General Agreement on Tariffs and Trade (GATT), that instead focused its negotiations on trade matters.[1] Only in the context of the Uruguay Round (1986-1995) were FDI issues brought again to the fore, as part of a series of agreements (some with an explicit investment content) that underlied the inception of the World Trade Organization (WTO), such as the Agreement on Trade-Related Investment Measures (TRIMs), the Agreement on Trade-Related Intellectual Property Rights (TRIPs), the General Agreement on Trade and Services

[1] Between the 1940s and the 1990s, there were however a range of initiatives at the OECD and UN level, notably the binding codes of the OECD on Liberalization of Capital Movements and Current Invisible Operations (1963), the voluntary OECD Guidelines for Multinational Enterprises (1976, and regularly updated), the draft (voluntary) UN Code of Conduct on Transnational Corporations (submitted in 1990 but not finished). More recently, the draft OECD Multilateral Agreement on Investment (MAI), which aimed to provide a comprehensive multilateral framework, had its negotiations suspended with no agreement. For a more thorough historical account of investment-related rules, see Brewer and Young (2000), and Gugler and Tomsik (2007).

(GATS), the Agreement on Subsidies and Countervailing Measures (SCMs), and the Agreement on Dispute Settlement Understanding (DSU). Nevertheless, these agreements seem to address investment only in a collateral way, meaning that they were not designed specifically with investment issues in mind (Sauvé and Wilkie, 2000; Young and Tavares, 2004).

More recently, and within the scope of the WTO, FDI-related matters were brought again to the discussion. The Doha Round (launched in November 2001) explicitly included investment themes in (among others) negotiations related to the GATS, the TRIPs Agreement, in the Antidumping and Subsidies Agreements, and even special working groups were set up in order to study the relationship between trade and investment, between competition and investment, and on transparency in government procurement. Progress with the Doha 'Development' Round has been far from pacific and smooth, and suffered a serious setback in Cancún, 2003, when the 5th Ministerial Conference of the WTO ended abruptly, with a group of developing countries walking out of the negotiations. Since then, investment issues keep being mentioned, but without much progress, and prospects for a multilateral investment agreement seem as unlikely as ever (Young and Tavares, 2004).

In all, and as often stated there is probably no better word to describe the current situation regarding international investment regulation than 'patchwork'. We just briefly characterized the situation at the multilateral level. However, the architecture of international investment regulation is more multi-level and complex than that. Various overlapping levels coexist and interact, often being contradictory – hence leading to a manifest lack of systemic coordination (Tavares, 2001). There are investment rules at the multilateral, regional (trade / investment blocs), bilateral / national, and even sub-national levels. The sophistication and depth of such rules is highly variable among levels, and even within the same level (Young and Tavares, 2004).

Presently, the most important instrument for the international protection of FDI is at the bilateral level. Bilateral Investment Treaties (BITs) have proliferated immensely in recent years – according to the latest *World Investment Report*, there are already more than 2500 BITs in place (UNCTAD, 2006).[2] Such proliferation, and clear preference for a bilateral approach can be explained by the lack of measurable benefits from the existence of a multilateral framework, *vis-à-vis* the reduction of government discretion / autonomy and the high adjustment costs perceived to be implied by multilateralism (Lengyel and Ventura Dias, 2004). BITs have existed since 1959, and are seen as specifically relevant when host countries institutions and property rights are weak. Put very simply, they mainly aim to protect subsidiaries of MNEs from discrimination, grant national- and most-favoured nation treatment, protect from risks like expropriation, capital transfer restrictions, losses due to war, etc. Countries signing them expect to have greater FDI inflows. However, studies testing the relevance of BITs as FDI determinants have not found a significant influence on such agreements on FDI inflows, hence questioning their real effectiveness (UNCTAD, 1998: Hallward-Driemeier, 2003).

There is also considerable diversity at intermediate levels between fully-fledged multilateralism, and outright bilateralism. In this vein, a vast array of agreements at the plurilateral and regional levels are in place, thus contributing to a more diverse and complex picture. Examples are the agreements at the level of the NAFTA, OECD, APEC, among others (for a more comprehensive review, see Brewer and Young, 2000; Kennedy, 2003, Gugler and Tomsik in this volume).

Another aspect that needs to be taken into account and one that does not make this 'fabric' of IIAs tighter and more coordinated is the tough competition for FDI (Tavares and Young, 2003)

[2] For a more detailed overview of investment regulation at the bilateral level (as well as the regional and plurilateral levels) see the Chapter by Gugler and Tomsik in this volume. This chapter also addresses in detail relevant agreements covering investment-related issues such as the GATS, TRIPs, TRIMs, SCMs, among others.

that marked very strongly the last decade. In almost all countries (and even in many subnational jurisdictions), investment agencies were created, aiming to embark on the proactive attraction of FDI and subsidiaries of multinational firms. This meant developing (sometimes more successfully, sometimes less) a strategic approach towards attracting FDI, trying to differentiate their 'locational product' and hence trying to retain all possible discretion in terms of providing the maximum possible amount of incentives of several kinds. This means an adverse context towards policy coordination (e.g. fiscal) and surrender of sovereignty over policies adopted, and over the generous incentives offered to MNEs. In particular, developing countries seem to be quite adverse to the idea of being forced to harmonize their policies with those of their developed counterparts, given the high expected adjustment costs, the loss of sovereignty implied, and the likely inability to undertake domestic reform because of the implacable adjustment path required, that may impede such countries to focus on national priorities. Countries want control over pace, sequencing, and liberalization of reform (Young and Tavares, 2004).

Even if most countries, developed and developing alike, are ready to give generous incentives to MNEs, research has questioned the efficiency of such incentives, and the positive net impact of many subsidy-induced FDI operations (for a deeper analysis, see Tavares and Young, 2005). This would bring back the pertinence of pondering the advantages of a broader FDI-related agreement, thereby avoiding the deadweight losses implied by escalation in this tough race (sometimes even within countries, and within the same regionally-integrated bloc). It is not the aim of this paper to debate all pros and cons of a broader (specifically, multilateral) investment agreement[3]. However, it is interesting to observe how the policy pendulum has swung over the years, which is the objective of the subsequent section.

[3] This is done to a certain extent in Young and Tavares (2004).

3. THE SHIFTING POLICY PENDULUM

Since the 1940s, the policy pendulum between the forces for regulation and those for liberalization has swung considerably. The following Figure charts the pathways underlying this policy pendulum.

[FIGURE 1 ABOUT HERE]

From the time of the Havana Charter until the late 1960s, liberalization tendencies were moderate towards weak (at the latest part of this phase). Forces for regulation were weak, meaning that, probably owing to its newness and relative incipience of the idea, the establishment of investment rules did not command great passions.

The situation changed considerably in the late 1960s, in a phase that lasted until the early 1980s. This era, marked by economic crisis worldwide (with the oil shocks and the ensuing recession) represented a hostile environment for FDI. In particular, forces for regulation dominated, and FDI was rather controlled than left to its own devices.

The early 1980s saw a major turnaround in this environment and, until the mid-1990s, the context was one of liberalization, with very weak pro-regulation forces. It reprsented the 'liberal era', not only in investment, but also in trade and related issues. Markets were king.

The last years (late 1990s-early 2000s) witnessed an increase in the strength of forces towards regulation, although still in a context of strong liberalization tendencies. However, it seems that at present liberalization tendencies are weakening, being plausible to propose that an increasing

'controlling' trend might emerge, given the impact of some 'new' issues on the FDI policy agenda (such as environmental concerns, human / labor rights, corporate social responsiblility [CSR], among others). The growing awareness of these issues is in great part due to the increasing power and impact on the public opinion of new actors / pressure groups, like the variety of non-governmental organizations (NGOs) and other movements.

It is pertinent to question why such path occurred since the 1940s until the present, and the theoretical and practical reasons underlying how we got to where we are. If in the first phase (1940s-late 1960s) there was a relative indifference as FDI-related policy was not yet very high on the agenda. In the late 1960s and especially in the 1970s and early 1980s the situation moved towards a stiff controlling stance given aspects such as the protagonism and growing importance from US and later European and Asian MNEs, that scared countries that did not expect such protagonism. Other reasons were the global recession due to successive oil shocks, and the dominant political, ideological and political economy perspective on 'dependency' and 'imperialism', especially against the US and US multinationals. In this phase, bargaining models (Fagre and Wells, 1982; Lecraw, 1984; Kobrin, 1987) were developed in order to understand relations between MNEs and developing country governments, confrontational and tense at that time. The first generation of these models, dating from the 1960s-1970s, depicted a situation where there was a one-to-one negotiation between a MNE and a government, with the specific entry terms depending on the relative power of the bargaining agents (Ramamurti, 2001; Young and Hood, 2003).

From the early 1980s until the mid-1990s, there was a tremendous shift towards liberalization, following the influence of liberal regimes in the US, the UK and other countries, the changed perception that MNEs would usually bring positive spillovers to the host economy, and the lack

of popularity of traditional bargaining frameworks – all this contributed to a very explicit liberal stance, and a positive perspective on the contribution of MNEs.

Finally, in the late 1990s, early 2000s, the situation is again shifting, though it is not clear exactly where it is going to end: the context is one of strong liberalization tendencies, yet these are weakening, and allowing more controlling arguments to gain currency. This led to a 'second generation' of bargaining models (Ramamurti, 2001)[4], that take into account the increasing bargaining power of MNEs (that can leverage and capitalize the advantages of the spread of their value chains and sophisticated international production systems), the decreased power of nation-states (all desperate to attract FDI, thus making incredible concessions to MNEs), and the multi-level, multi-party potential of the bargain. It is not uncommon at present to read reports of MNEs playing states against one another, in order to squeeze the maximum of investment incentives (Ghauri and Oxelheim, 2003).

This recent evolution, encompassing a 'cautious' shift towards less liberalization and possibly greater controlling proclivity cannot be divorced from the current debate regarding globalization and its effects, and the scepticism that globalization will always be 'good' (Stiglitz, 2002). The increasingly vociferous civil society (that manifested itself especially after the WTO Ministerial Meeting at Seattle in 1999, where anti-globalization movements - as we know them now - gained prominence for the first time) is amplifying the need to question the benefits of globalization (and their ultimate actors, MNEs), and pushing towards greater regulation and control.

[4] For a more thorough development of bargaining power arguments, and competition can be replaced or complemented by cooperation see Young and Hood (2003), where these authors propose an 'alliance compact' between companies and countries.

The advent of new / emerging issues not traditionally taken account in the FDI-regulation debate is contributing to shift this pendulum more towards a careful, not so liberal, stance *vis-à-vis* investment rules. This stems in great part from the potential adverse effects perceived to be implied by the operation of MNEs in host countries (and often their supranational, transborder impact), in areas like the environment (e.g. climate change), competition policy, human / labor rights, among others, that will be developed in the next section.

4. ISSUES FOR INCLUSION IN IIAS TO BALANCE RIGHTS AND OBLIGATIONS OF COMPANIES / COUNTRIES

The range of issues that entered the debate recently is very encompassing.

Recent initiatives (such as the MAI and the UN Global Compact) have been calling attention to formerly neglected aspects pertaining to these 'new issues'. The MAI (abandoned in 1998) already considered the development dimension of investment agreements (in this case, at the multilateral level), as well as referring to environmental concerns, and human and social rights. The UN Global Compact (launched in 1999 [UN, 2000]), launched to promote global corporate citizenship, embraced 10 principles, including those related to human rights (principles 1 and 2), environment (principles 7 to 9) and anti-corruption behaviour (principle 10).

The inclusion of these 'new' issues resulted from reality (reflecting the importance given to such matters and the questioning of simple truths such as that spillovers from FDI are always positive, as well as a more informed stance about imminent degradation of natural and, in some cases, of human conditions).

What needs to be understood also is that in the past, the FDI-related framework (especially at the dominant, bilateral level) emphasized mainly the rights of companies and the obligations of host countries *vis-à-vis* such firms. The latter tended to gain more and more power, making some

governments (especially from small and/or developing countries) virtually incapable of negotiating in a fair and balanced way with such firms. This created a growing sense of uneasiness in many nations, that manifested itself quite strongly in the fiasco of the Cancún negotiations in 2003, when a group of developing countries abandoned the table, for several reasons, among which disagreement over investment regulation was important.

The current consciousness that the quality of the environment is a growing concern, that labor / human rights are experiencing degradation in many circumstances, that globalization is promoting efficiency quite reasonably, yet not always in an equitable or 'developmental' way, that multinationals often embark on anti-competitive practices, both in terms of increasing unhealthily market power, and / or adopting dumping behaviour to destroy domestic companies, is leading to a more careful consideration of a range of issues that were absent from the traditional agenda. These issues are varied and complex, and include:

- Balancing efficiency and equity
- Economic development and poverty reduction
- Sustainable development
- Environmental rules (particularly climate change)
- Labor and employment rights
- Human rights
- Competition policy and restrictive business practices

Balance between efficiency and equity / Economic development and poverty reduction

As regards the balance between efficiency and equity, there are some doubts whether the seemingly more efficient allocation of resources promoted by globalization is leading to a more equitable outcome (Hirst and Thompson, 1996; Stiglitz, 2002). The active debate on globalization highlights the possibility of asymmetric costs and benefits to different actors, and of a potencial widening gap between gainers and losers. Asymmetries on the international distribution of income – particularly between developed ad developing nations – are often alluded to, as well as disparities on the distribution of the income by social group.

This issue scan be linked to the contribution of FDI to economic development and poverty reduction. The fact that MNEs lead to positive spillovers to the local economy, hence performing a 'developmental' role has often been debated. Indeed, the vast literature on FDI impact led to mixed results (for a review see Görg and Strobl, 2002; Tavares and Young, 2005). Moreover, the effect of multinationals' activities on the domestic distribution of income is also unclear. As regards strictly the impact of multinationals on wages, the empirical literature mainly concludes that MNEs pay greater wages than their domestic counterparts (Brown et al, 2003; Velde and Morrissey, 2003; Görg et al, 2007) – therefore, leading in principle to poverty reduction. For instance, the paper by Velde and Morrissey (2003) is a study based on 5 African countries. Focusing specifically on wage inequality, Figini and Görg (2007), in an empirical study using Irish data, found evidence in favour of an inverted-U relationship between wage inequality and the presence of multinationals, i.e., with increasing presence of MNEs, wage inequality first

increases, reaches a maximum and decreases eventually, *ceteris paribus*.[5] Hence there are still concerns that MNEs may lead to increased inequality.

Environmental rules (particularly climate change); Sustainable development

Environment and sustainability are key themes nowadays, for developed and developing countries. The growing consciousness that human activity is producing irreparable damages on the environment is making actors (individuals, organizations, givernments alike) rethink the way they lead their lives. The effects of climate change, in particular, are obvious and a cause for deep concern.

Although this is not *per se* and specifically a FDI-related issue, it will have an impact on the way MNEs operate, and will mean that stricter environmental compliance rules will tend to be imposed. This, again not a FDI-specific theme, and not even one within the remit of the WTO, will mean that we need here also to promote a fairer balance between the obligations of companies and rights of countries, in the vein argued in this paper. Some less-scrupulous MNEs will relocate where they undertake environmental dumping, and where they can obtain permission for greater CO_2 emissions. The possibility of having a great allowance for emissions is even heralded as a kind of FDI incentive.

However, the Kyoto Protocol and the growing strength of the NGO / consumer lobby is putting pressures on MNEs in this area, as they did successfully in respect of corporate social responsibility (CSR).[6] MNEs are already responding to these pressures (Kolk and Pinkse, 2007).

[5] This study aimed to test the Kuznets (1955) hypothesis, according to which, in order to increase economic growth and development, income inequality has first to increase, then decreasing at a later stage.
[6] More on CSR in section 5 in this paper.

Labor and employment rights; human rights

Another controversial area relates to the potential negative contribution of MNEs to labor/employment rights, and even to human rights, in some cases. Indeed, it has been argued that MNEs, often due to the growing competitive pressure they face worldwide, and especially in the main markets and in the most dynamic sectors, are becoming increasingly obsessed with cost reduction, doing whatever they can to save on aspects such as social contributions, and other benefits given to their workers. The restructuring of key industries is prompting successive waves of mergers and acquisitions (M&As) with a considerable employment impact, implying massive shedding of workers. MNEs are often accused of effecting social dumping, having no respect for workers' rights. However, and even if they can correspond to the truth in a considerable number of cases, these concerns are often rejected by studies on developing countries that defend MNEs (which, apart from paying better wages as we saw before provide better working conditions than their local counterparts). Furthermore, it is argued that multinationals are typically not attracted preferentially to countries with weak labor standards (Brown et al, 2003). As the same study (pp52-53) notes "However, as an empirical matter, some anecdotal evidence notwithstanding, there is virtually no careful and systematic evidence demonstrating that, as a generality, multinational firms adversely affect their workers, provide incentives to worsen working conditions, pay lower wages than in alternative employment, or repress worker rights. In fact, there is a very large body of empirical evidence indicating that the opposite is the case. Foreign ownership raises wages both by raising labor productivity and expanding the scale of production, and, in the process, improving the conditions of work". Civil society groups can still point to company-specific examples where exploitation appears to have occurred, and hence labor and human rights need to continue to be vigorously defended.

Competition policy and restrictive business practices

Multinationals are ofte accused of having an anti-competitive behavior, both in terms of building strong market power (in the limit, leading to monopolies), as well as in terms of undertaking dumping and predatory pricing practices to anihilate domestic competitors. This is a cause for preoccupation especially in the case of countries with weak industrial structures and weak indigenous industrial fabric, whose domestic firms cannot withstand the competition from their foreign (stronger) counterparts. It is thus an issue particularly applicable to developing nations.

Gugler and Tomsik (2007) refers to these issues, specifically to the potential impact of FDI on competition, and on how competition (and specific themes such as cartels) was included in former steps in the international investment regulatory agenda. Some BITs and regional agreement investment provisions (such as those of the NAFTA) tackle anti-competitive practices, such as cartels. However, cartels are often global phenomena, beyond the reach of bilateralism and regionalism. Thus efficient treatment of them would occur only at a multilateral level, thereby avoiding arbitrage between jurisdictions as well.

Recently, national and regional competition authorities proliferated. Even if the actions of these national competition authorities can be potentially quite effective, some need for coordination exists – the issue is then if such cordination is more informal, voluntarily done between authorities, or more institutionalized (e.g. through a Competition Policy Committee as Gugler and Tomsik suggest earlier in this volume). For instance, the NAFTA Working Group on Trade and Competition could provide an inspiration for this.

In respect of developing countries, competition policy is one area where proposed amendments to special & differential treatment (see proposals by Hoekman et al, 2004 below) would remove

reciprocity requirements because of the high costs and limited benefits from implementing anti-trust rules.

5. OPTIONS FOR PROGRESS

Emerging from the above discussion, it is evident that ways have to be found to improve the balance in the global trade and investment framework. This requires greater obligations for firms and increased rights for countries, especially developing nations, within a context in which the basic principles of global liberalization threaten to be undermined by the growth of bilateralism (and potentially regionalism), on the one hand; and the emergence of new issues such as the environment, human rights, sustainable and equitable development. A number of options for progress are now considered.

Rules-based multilateralism - a sector-specific approach

The discussion above has indicated that progress on investment agreements in the WTO may not be possible or desirable (Young and Tavares, 2004). Nevertheless, there already exists one WTO agreement which incorporates FDI, namely, the General Agreement on Trade in Services (GATS), established in 1994. Why has it been possible to introduce FDI into the GATS but not more widely within the WTO? There are several explanations. First, in a number of service sectors, products are non-tradable, meaning a requirement for foreign direct investment to supply markets. Second, there is evidence that FDI is beneficial for host economies, as a source of new knowledge and competitive stimulus, and because FDI may assist host countries to introduce and export more advanced products (Hoekman, 2006; Markusen, Rutherford and Tarr, 2005). Third, it is argued (Bhattari and Whalley, 1998) that the distribution and size of the gains from market

integration may be more equally shared between large and small countries in services than in goods.

Given the importance of the services sector in national economies (representing between 35% of GDP in lowest income countries and over 70% in the OECD countries – Hoekman, 2006) and in global FDI flows (72% in 2001-2002 according to UNCTAD, 2004 estimates), a multilateral agreement clearly represents an important step forward. In addition, the productivity of the services sector is of significant for the growth prospects of countries. For example, research by Mattoo, Rathindran and Subramanian (2006) estimated that economies with open financial and telecommunication sectors grew about 1 percentage point faster than others. Full liberalization was associated with an average growth rate 1.5 percentage points above other nations. Much less information is available for developing countries. However, in a study of 86 developing countries in telecommunications, Fink, Mattoo and Rathindran (2003) found that a comprehensive reform program, including both privatization and competition and supported by an independent regulator, produced a 21% higher level of labor productivity compared to years of partial and no reform. This study covered the period 1985-99, while the big stimulus likely to be generated by mobile phones is essentially a phenomenon of the 2000s.

Despite the apparent benefits of a multilateral regime incorporating FDI, the GATS has apparently played only a limited role in liberalization processes. Hoekman (2006) suggests that because of the importance of domestic regulatory policies, the incentive for unilateral reform may be larger in services than in goods; and he concludes that excluding EU members, most reforms have been undertaken by countries autonomously. There can still be a role for the WTO in supporting the implementation of reforms. Thus Hoekman and Mattoo (2006) argue the case for using the WTO to assist developing countries in assessing the state of their service sectors; in providing assistance to support liberalization; and in monitoring the delivery and effectiveness of

reform. By this means the GATS could become a mechanism not just to promote services liberalization but also to assist domestic services reform. In respect of FDI there are still many barriers both in terms of ownership limitations and operating restrictions.

Service industries will continue to grow rapidly and are a key determinant of firm competitiveness because of their ubiquitous nature. So even in the manufacturing sector the service content is rising because of the importance of value chain activities such as R&D, design, finance, and sales, marketing & distribution. To date the GATS has not had an important role to play in FDI liberalization, but into the future an enhanced role should not be discounted.

Multilateralizing regionalism

There is a longstanding debate concerning whether regional integration agreements (RIAs) are complementary or competitive in terms of their role in liberalizing the world economy (Kobrin, 1995; Brewer and Young, 2000). The fact is that such RIAs exist and are likely to become more important into the future, as existing arrangements, particularly the EU and NAFTA, expand membership and extend their 'hub and spoke' systems. The future in East Asia is more questionable. Certainly there are numerous initiatives under negotiation or already signed, including, for example, the ASEAN-China Free Trade Area (FTA), the ASEAN-Korea FTA and the ASEAN –Japan FTAs., but these are relatively undisciplined and there are calls for binding the unilateral tariff-cutting within the WTO system (Baldwin, 2006).

In respect of improving a balance in the rights of countries within multilateral agreements there is an argument for suggesting that RIAs may actually help to achieve this. Thus the relatively greater homogeneity of countries within regional blocs may make it easier to achieve a common bargaining position than in the more heterogeneous WTO. And the route to trade and investment liberalization for the global economy is rather similar to that for a particular region. A contrary

perspective is that while RIAs liberalize internally, they may lead to a world of regions which are more restrictive against trade from outside the bloc and which could generate trade wars. However the main three blocs of Europe, North America and East Asia all have 'leaky and 'fuzzy' boundaries (Baldwin, 2006) such that potential protectionism may be circumvented by multinationals as they seek to secure their supply chains which are not only regional but also global.

As RIAs evolve alongside the WTO, there is a need for mechanisms to ensure greater coordination and integration between the forms of institutions. Suggestions have been made (Hoekman and Kostecki, 2001; Brewer and Young, 2000) to strengthen the process of examining agreements; to establish multilateral rules relating to accession clauses in RIAs for new members (especially for associate status countries); and to strengthen multilateral disciplines in respect of rules of origin for RIAs. In reality, according to Baldwin (2006): 'The WTO has been little more than an "innocent bystander" in the massive spread of regionalism'. In order to make progress, Baldwin (2006) has suggested focusing more on improving information and coordination as a less contentious way of progressing towards the long-term goal of 'multilateralizing regionalism' (that is incorporating and integrating RIAs within the global framework of the World Trade Organization). Three roles are suggested for the WTO: First, providing clearer information and a better informed understanding of the effects of multilateralizing regionalism. Second, establishing a negotiating forum for the standardization and harmonization of rules of origin. The third proposal is particularly relevant to this paper because of its focus upon hub and spoke relationships. There are potentially large asymmetries in bargaining power especially between small nation RIA spoke partners and large hubs such as the EU or NAFTA when the former may be dependent on the hub market. The suggestion, therefore, is for the WTO to establish a forum of 'spoke countries'. The objective would be to set up an advisory centre focusing upon North-

South and South-South RIAs (where the WTO's Advisory Centre on WTO Law might be used as a model) to improve the knowledge and skills of spoke members in negotiations. Since RIAs are here to stay and their importance in the global economy likely to increase, efforts to multilateralize regionalism represent are important alongside other measures in efforts to balance rights and obligations.

Rules-based approach, with gradation of rules

There are already amendments to the principle of universality within the WTO, as represented by special and differential treatment (S&DT) for developing nations. This was incorporated into the GATT in 1979, permitting preferential market access for developing countries, limiting reciprocity in negotiating rounds to levels 'consistent with development needs' and providing developing countries greater freedom in trade policies than would otherwise be allowed by GATT rules (Hoekman, Michalapoulos and Winters, 2004). There has been much criticism of S&DT, in part related to wider criticisms of import-substituting policies in developing countries. Their value has also been questioned since tariff-cutting in successive negotiating rounds has diminished the preferences for developing countries. Furthermore, sectors of major importance to developing countries like agriculture and textiles & clothing were excluded from the GATT and dealt with on an ad hoc basis.

In any event the pressures to take greater account of development needs surfaced at the end of the 1990s as part of wider criticisms of multinationals and global capitalism, and the failure to launch a new Millennium Round of trade negotiations (Brewer and Young, 2000, p277-279). After much acrimonious discussion, the Doha Round of negotiations was eventually launched in 2003 as a so-called 'Development Round' (see Hoekman, 2002). In the Doha Ministerial Declaration there was a call for a review of the S&DT provisions to strengthen them and make them 'more precise,

effective and operational' (para. 44). Progress since then has been patchy to say the least and the 2003 deadline for agreeing new provisions was not achieved.

In a subsequent paper, Hoekman et al. (2004) presented some ideas for progress, focusing upon, first, improvements in market access; second, rebalancing existing agreements, such as agriculture, and amending others; and, third, development assistance to build institutional and trade capacity. The starting point is a redefinition of the countries to be permitted S&DT. The current WTO classification distinguishes between LDCs, other developing countries and developed economies. These authors propose that only a sub-set of developing countries should be eligible, namely the LDCs plus 'other low income and small developing countries with weak institutional capacity' (Hoekman et al, 2004, p504). This is a strongly desirable reform, albeit also very politically sensitive.

In relation to the first issue above, the recommendation is to expand market access through the abolition by industrial countries of export subsidies and non-tariff barriers for labor-intensive products of interest to the poor and small developing countries group. The tariff target is 5% in 2010 and zero in 2015 (the date set for the achievement of the Millennium Development Goals). It is recognized that some (although not matching) reciprocal concessions will be necessary by the poor and low income countries. The latter is clearly a big issue for negotiations.

The second issue concerns agriculture and amendments to other agreements. The proposals to rebalance the rules in agriculture would involve allowing special safeguards for low income countries, specifically emphasizing measures to improve food security and to stimulate agricultural production of the poor in rural areas. Amendments to rules would focus upon removing of reciprocity requirement in policy areas that are costly and resource-intensive to implement or are not development priorities for poor and small developing countries (and where

in truth the effects upon developed country investors are likely to be quite small). These policy areas might include TRIPS, customs valuation, competition policy and procurement.

The third set of proposals by Hoekman et al (2004) concern development assistance to build institutional and trade capacity and enable poor countries to benefit from improved access to industrialized country markets. Such assistance to build supply-side capacity and capabilities and improve trade mechanisms, as well as assisting technology development is essential if poor countries are to benefit from liberalized markets. Since the assistance has to be tailored to individual country needs, there are issues to be resolved concerning what assistance is to be provided and to which countries; whether or not this will be linked somehow to the implementation of WTO agreements (Finger and Schuler, 2000); and the relationship with bilateral donor support schemes which commonly address supply capacity and trade support measures.

Combined rules-based and voluntary approach

The possible options for progress outlined above do not in the main tackle the basic requirement for improving the rights of developing countries. The exception concerns the proposals by Hoekman et al (2004) for deepening special and differential treatment for the key group of the poorest and small countries. And even here it appears that country-specific solutions will be required in implementing the recommendations on building supply-side capacity and improving trade mechanisms.[7] In the light of this, it is worth considering the potential for taking a different approach to some of the developmental challenges facing poor countries, focusing upon voluntary initiatives from both public policy (at different levels) and from multinational firms.

[7] It is beyond the scope of this paper to consider multilateral institutional alternatives to the WTO to handle important global issues like the environment, labor and human rights issues etc, but, for example, an organization such as the International Labor Organization (ILO) is an obvious player in respect of labor matters.

The growing interest in voluntarism derives in significant part from the notion of CSR which is crucial to the management of the costs and benefits of business activities to stakeholders, both internal (employees, shareholders, investors) and external (public governance organizations, civil customers, suppliers, other enterprise, civil society) (Fox, Ward and Howard, 2002). CSR has emerged as a major agenda item for firms and governments because of the risks and social consequences of globalization for developing countries. The World Business Council for Sustainable Development (WBCSD, 2002) defines CSR as: 'The commitment of business to contribute to sustainable development, working with employees, their families, the local community and society at large to improve their quality of life'. What is particularly interesting in the context of this paper, is the observation by Fox et al (2002, p1) that 'there is a dynamic linkage between voluntary approaches and regulation and the potential for voluntary initiatives of various kinds to crystallize, over time, into mandatory minimum standards'.

There are a large number and range of voluntary initiatives operating at different levels (multilateral, regional, national and sub-national) and involving public institutions, governments and firms. Space does not permit commentary on all these non-binding initiatives, and so a number of illustrations will be presented.

From the international public policy perspective, codes of conduct or guidelines for MNEs were much in vogue during the regulatory era of the 1970s.. Among such voluntary initiatives, *The OECD Guidelines for Multinational Enterprises* (1976/2000) (www.oecd.org/daf/investment/guidelines) was a significant initiative to set principles and standards for responsible business conduct by MNEs in areas including information disclosure, employment and industrial relations, human rights, environment, science & technology, combating bribery etc. The OECD Guidelines have been updated regularly, most recently in 2000. From the same era is the ILO's *Tripartite Declaration of Principles Concerning*

Multinational Enterprises and Social Policy (1977) (www.ilo.org/public/english/employment/multi/index.htm) which provides guidelines for MNEs, governments, and employers' and workers' organizations in the areas of employment, training, conditions of work and life, and industrial relations. A much more recent initiative is the United Nations *Global Compact* (www.unglobalcompact.org), launched in 2000 with the aim of promoting global corporate citizenship. Specifically the Global Compact's ten principles focus upon human rights, labor standards, the environment and anticorruption with the involvement of 3,800 participants including 2,900 businesses from 100 countries along with representation from UN agencies, labor and civil society.

While these various initiatives are partly complementary, there are also significant areas of overlap in terms of participation and coverage. The OECD Guidelines are implemented through the member governments of the OECD together with a number of non-members, and a co-operative project has been launched to improve business governance via the Guidelines in China and by Chinese MNEs. The ILO Declaration is narrowly focused upon employment, working conditions and industrial relations aiming at a wide range of participant organizations. The UN Global Compact is designed as a network-based initiative with a multi-tier governance framework operating at both global (Global Compact Leaders Summit) and local network levels. The Local Networks, currently 50 in number, comprise groups of participants within a particular country, whose role is to assist local firms and MNE subsidiaries in the implementation of its ten principles, and to root the Global Compact within different cultural contexts.

It is debatable how significant these multilateral initiatives are. The OECD Guidelines probably suffers from its association with regulation-oriented 1970s era, and its developed country sponsorship may be a negative at the host (developing) country level. Forty-one percent of the respondents to a 2006 survey of the Fortune 500 companies indicated that their companies 'use

the Guidelines as a reference'.[8] The genesis of the ILO Declaration may create similar negative perceptions, as might its focus upon labor issues. The UN Global Compact is by comparison wide in coverage and more inclusive in terms of participation. Its decentralized operational approach is valuable too, something which has also been implemented by the OECD through its mechanism of National Contact Points (NCP).[3] What is perhaps most important is that there are now attempts to coordinate activities among the three multilateral institutions within an international CSR framework.

There is little doubt that CSR (and the associated pressure from shareholder groups, civil society and other stakeholders) has altered MNE perspectives towards developing countries. An OECD survey at the end of the 1990s identified 233 codes of conduct, setting out behavioral standards that companies pledge to follow (primarily CSR principles), most of them relating to individual firms (www.oecd.org//ech/act/codes/ht; see also Brewer and Young, 2000, p284 for a brief review). NGOs have been skeptical of codes, viewing them as mere public relations exercises; and certainly if they are to be effective, they have to more than altruism and philanthropy. Interestingly Husted and Allen (2006) found that local CSR issues were more likely to appear on the strategic agendas of multidomestic and transnational rather than global MNEs. However, there is at least anecdotal evidence that within large MNEs the CSR units may be organizationally separate from the product divisions and hence not integrated into mainstream corporate activities. Nevertheless, there are positive signs, with illustrations in Africa, for example, of MNEs either singly or in groups seeking to integrate local suppliers within their regional as well as local supply chains.[9] One interesting initiative in this regard is *Business Action*

[8] See 'The Contribution of the OECD Guidelines for Multinational Enterprises to Managing Globalization' (www.oecd.org/dataoecd/5/34/38543990.pdf).

[9] This information was obtained from an UNCTAD Expert Meeting on Best Practices and Policy Options in the Promotion of SME-TNC Business Linkages, Geneva, 6th – 8th November 2006, attended by one of the authors.

for Africa (www.businessactionforAfrica.org).[10] which focuses upon the six themes of governance and transparency, trade, the business climate, enterprise and employment, human development, and perceptions of Africa.

6. CONCLUDING REMARKS

What appears to emerge from all of this is that the major challenge in improving the rights of countries and the obligations of firms lies less in multilateralism and the WTO than in country-specific initiatives, which are in our view outside the remit of the World Trade Organization. We are supportive of new proposals in respect of S&DT within the WTO which are designed to address difficulties facing all developing countries (specifically the poorest and smallest developing nations). But country-specific programs are a step too far for the WTO, especially when there are already large numbers of initiatives at the country level undertaken by other multilateral institutions (e.g. World Bank, IMF), regional organizations (e.g. EU), and national governments. At all of these levels there is a requirement for greater integration of effort to limit competition and confusion, and improve coordination and clarity. As has been argued elsewhere, 'the hierarchical donor-recipient of most aid programs has to be replaced by collaborative relationships with national governments in developing countries; this, in turn, requires a planning framework for prioritizing and directing donor resource allocations' (Young and Hood, 2003, p268).

A problem which still remains concerns the limited capacity and capability of developing country bureaucracies to implement the initiatives which emanate from foreign donor agencies. In some ways the direct involvement of multinationals with host developing countries (at firm but also

[10] Its corporate sponsors are Anglo American, BAT, De Beers, Diageo, International Business Leaders Forum, MSD, SABMiller, Shell, Unilever and Visa.

government levels) is helpful since it is hands-on and business-related. This is very obviously the case with supplier linkage programs where an element of training is almost inevitably involved. However a feature of MNE activity (especially large Western multinationals) is their involvement in wider aspects of private sector development such as sectoral training initiatives, advice on trade and investment policy, investment promotion and after-care etc.

Young and Hood (2003) have proposed the notion of an 'alliance compact' between MNEs and developing country governments as an evolving partnership, taking the form of a non-binding semi-formal agreement between parties, updated annually. It is suggested that the MNE affiliate-host country agreement would be prepared on an individual company basis, recognizing that only a small group of the largest MNEs would be involved, at least in the first instance. The idea has some similarities with, for example, the *Business Action for Africa* initiative discussed above, but it emphasizes the implementation dimensions more strongly. In addition it is not top down in character, stressing instead collaboration and partnership.

In this paper we have attempted to consider ways of achieving a balance in the rights/obligations of firms/countries. Our view is that these go beyond the WTO's remit and require voluntarism alongside regulation. Of course it is important that the WTO remains as the central institution for liberalizing and regulating the global trade and investment system. Therefore reporting mechanisms have to be found to ensure that MNE-host country partnership activities are not totally divorced from the WTO.

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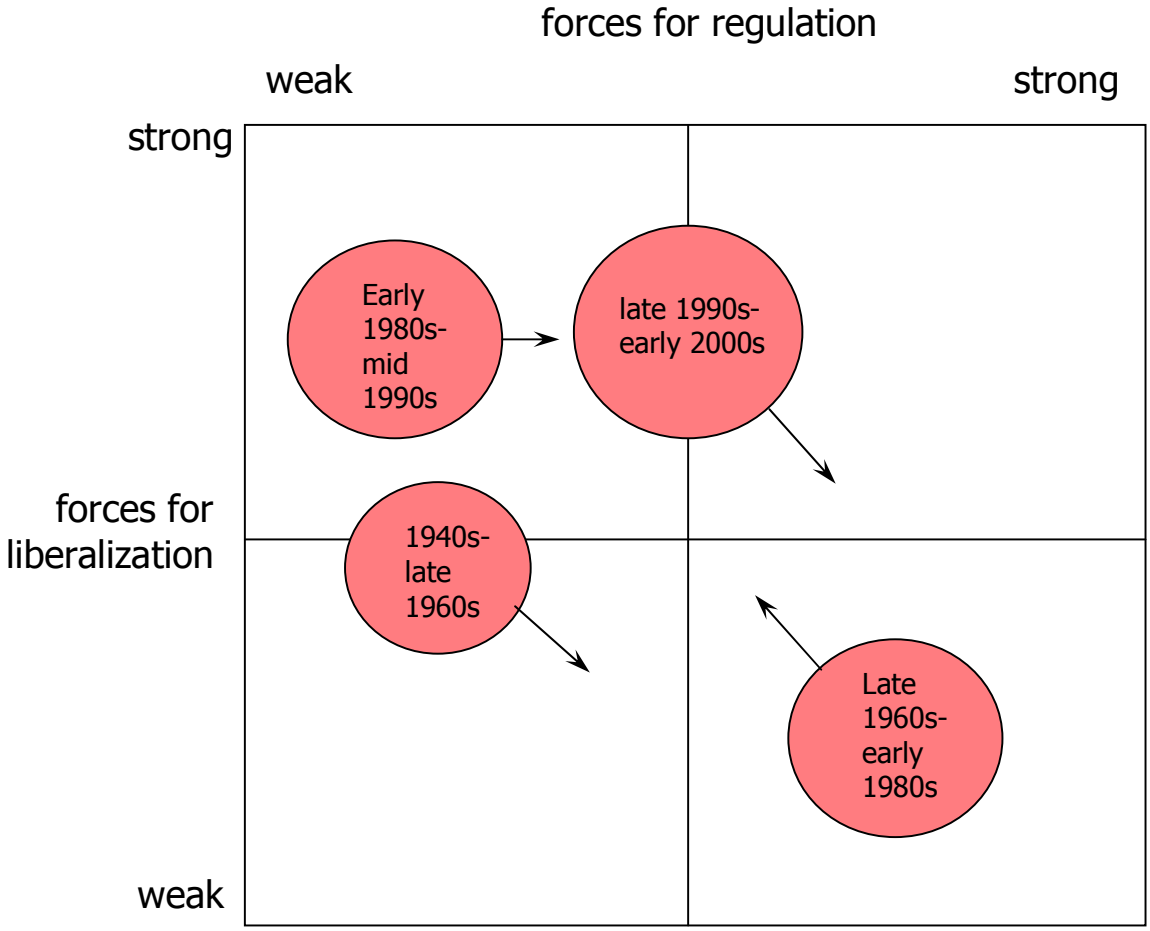
FIGURE 1. THE SHIFTING POLICY PENDULUM



Source: Brewer and Young, 2001.