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Codes of Conduct for Multinational Corporations: An Overview

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Congressional Research Service

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Codes of Conduct for Multinational Corporations: An Overview

Abstract

The U.S. economy has grown increasingly interconnected with other economies around the world, a phenomenon often referred to as globalization. As U.S. businesses expand globally, however, various groups across the social and economic spectrum have expressed their concerns over the economic, social, and political impact of this activity. Over the past 20 years, multinational corporations and nations have adopted voluntary, legally enforceable, and industry-specific codes of conduct, often referred to broadly as corporate social responsibility (CSR), to address many of these concerns. Recent events, primarily the 2008-2009 financial crisis and related work by major international organizations, spurred Congress and governments in Europe to increase their regulation of financial firms. Indeed, the growing presence and influence of multinational corporations in the production of goods and services and in international trade through value chains has prodded governments to adopt measures that enhance the benefits of such activities through codes of conduct. Congress will continue playing a pivotal role in addressing the various issues regarding internationally applied corporate codes of conduct.

Keywords

multinational corporations, globalization, corporate social responsibility, codes of conduct

Comments

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Codes of Conduct for Multinational Corporations: An Overview

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Summary

The U.S. economy has grown increasingly interconnected with other economies around the world, a phenomenon often referred to as globalization. As U.S. businesses expand globally, however, various groups across the social and economic spectrum have expressed their concerns over the economic, social, and political impact of this activity. Over the past 20 years, multinational corporations and nations have adopted voluntary, legally enforceable, and industry-specific codes of conduct, often referred to broadly as corporate social responsibility (CSR), to address many of these concerns. Recent events, primarily the 2008-2009 financial crisis and related work by major international organizations, spurred Congress and governments in Europe to increase their regulation of financial firms. Indeed, the growing presence and influence of multinational corporations in the production of goods and services and in international trade through value chains has prodded governments to adopt measures that enhance the benefits of such activities through codes of conduct. Congress will continue playing a pivotal role in addressing the various issues regarding internationally applied corporate codes of conduct.

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Background

Over the last decade, international flows of capital have skyrocketed and now total over \$6 trillion *per day*, or more than the total *annual* amount of U.S. exports and imports of goods and services. These flows are the prime mover behind exchange rates and global flows of goods and services. One part of these flows is foreign direct investment, or investment in businesses and real estate. On a cumulative basis, direct investment in 2011 totaled over \$20 trillion world-wide, about 20% of which is associated with the overseas investment of U.S. firms, the largest share held by the firms of any nation. Preliminary data for 2012 indicate that foreign investment flows both into and out of the United States slowed in 2012, reflecting a similar trend in world-wide investment data.

In addition to foreign direct investment in which firms take a direct equity stake in an investment project, multinational corporations are engaging in a broad array of activities, referred to as non-equity modes (NEM) of investment, that include partial ownership, joint ventures, contract manufacturing, services outsourcing, contract farming, franchising and licensing, and other forms of contractual relationships through which firms coordinate and control the activities of partner firms.¹ The United Nations estimates that NEM investment generated \$2 trillion in sales in 2010. While NEM investments can enhance the productive capacities of developing countries through integration into global value chains, employment in the affected industries can be highly cyclical and easily displaced.² Foreign investment spans all countries, industrial sectors, industries, and economic activities and has become a major conduit for goods, capital, and technology between the developed and the developing economies. Foreign direct investment has become a much-needed source of funds for capital formation in developing countries and foreign investment accounts for important shares of employment, sales, income, and R&D spending in developing countries.³

The United States is the largest recipient of foreign direct investment and is the largest overseas investor in the world, owning about \$4.5 trillion in direct investment abroad, or more than twice as much abroad as British investors, the next-most active overseas investors. This international expansion of business activity and overseas presence, however, often leads to a clash of cultures and values. In addition, conflicts are rising within the United States and within other developed countries over what role these global corporations should play in their respective home countries and over whose interests the corporations should serve. Traditionally, corporations have served the economic interests of a narrow group of shareholders by maximizing the return to the shareholders, or by maximizing the overall profits of the firm. Now, a broader group of “stakeholders,” including customers, employees, financiers, suppliers, communities, and society at large, is pressing for comprehensive codes of conduct that recognize their interests.

Defining codes of conduct is difficult, because such codes encompass a broad range of issues and myriad types of official and corporate activities that have defied attempts to reach a common agreement on the composition and nature of the codes. One way to view codes of conduct is by

¹ Non-Equity Modes of International Production and Development, *World Investment Report 2011*, United Nations Council on Trade and Development, 2011, pp. 123-176.

² *Ibid.*, p. 123.

³ *World Investment Report 2012*, United Nations Council on Trade and Development, 2012, p. 173.

grouping them into three main categories: (1) externally generated codes of conduct that are developed by governments or international organizations, (2) corporate codes of conduct that represent individual companies' ethical standards, and (3) industry-specific codes.⁴ These categories often overlap and some codes that initially were adopted voluntarily by companies or industries have been incorporated into law by governments. In other areas, there are notable gaps in the coverage of codes of conduct. Since congressional activities relate most specifically to the first type of codes, or externally generated codes of conduct, they receive the greatest emphasis in this report.

Congress has periodically considered issues related to corporate codes of conduct. In the 106th Congress, for instance, the House considered a measure (H.R. 4596) that would have required U.S. firms to adopt a Corporate Code of Conduct that covered a wide range of workers' rights and environmental issues, similar to the set of "model business practices" the Clinton Administration proposed in March 1995.⁵ Similarly, the Senate approved and the President signed on December 2, 1999, the Convention on Child Labor,⁶ which addresses various issues related to children in the workforce.⁷ The 106th Congress also considered a number of measures that addressed issues of child labor and the importation of goods produced with child, sweatshop, and prison labor. In the 108th, 109th and 110th Congresses, Congress considered various measures to protect children affected by poverty and natural disasters from trafficking, to protect children and minors from abusive labor practices, and to advance women's rights in developing countries. In the 111th Congress, Representative Maloney and Senator Boxer introduced companion pieces of legislation (H.R. 606 and S. 230, respectively) that would have promoted the international protection of women's rights. In the 112th Congress, Representative Maloney introduced H.R. 418 to promote the international protection of women's rights.

External Codes of Conduct

Since the 1970s, public and private expectations of multinational corporate behavior have grown commensurate with the boom in foreign investment. This change in expectations, however, has not resulted in a clear-cut set of directions for governments or businesses to follow in developing codes of conduct. At times, purely voluntary codes evolved into codes that subsequently were adopted as national legislation. For instance, in 1977, the United States adopted the Sullivan Principles and the Foreign Corrupt Practices Act (FCPA).⁸ Initially, the Sullivan Principles provided a voluntary set of standards for firms to follow to pressure the apartheid government of South Africa to improve the living conditions of black workers, their families, and their

⁴ Another way of categorizing business standards was developed by the United Nations, which uses four categories: 1) intergovernmental organization standards derived from universal principles; 2) multi-stakeholder initiative standards; 3) industry association codes; and 4) individual company codes. *Promoting Standards for Responsible Investment in Value Chains: Report to the High-Level Development Working Group*, Inter-Agency Working Group on the Private Investment and Job Creation Pillar of the G-20 Multi-Year Action Plan on Development, September 2011.

⁵ Administration's Draft Business Principles. *Inside U.S. Trade*, March 31, 1995.

⁶ Convention (No. 182) Concerning the Prohibition and Immediate Action for the Elimination of the Worst Forms of Child Labor, Geneva, June 17, 1999, entered into force November 19, 2000.

⁷ For additional information, see CRS Report RS20445, *Child Labor and the International Labor Organization (ILO)*, by Lois B. McHugh.

⁸ P.L. 95-213, Title I; 91 Stat. 1494, December 19, 1977. See also CRS Report RL30079, *Foreign Corrupt Practices Act*, by Michael V. Seitzinger.

communities. In 1986, Congress adopted the Sullivan Principles as law.⁹ The FCPA followed a series of congressional hearings and legal actions against numerous U.S. corporations,¹⁰ and specified legal standards and penalties that were meant to prevent U.S. firms from bribing foreign officials in order to gain economic advantages. Following the financial crisis of 2008-2009, the United States adopted the Dodd-Frank Wall Street Reform and Consumer Protection Act to address issues of governance and regulation of the financial sector, and the European Union has similarly adopted wide-ranging directives to improve oversight of the financial sector and to provide guidance on executive compensation. Also, as the United Nations has noted, “codes of conduct have become increasingly significant for international investment, since they typically focus on the operations of large multinational corporations which, through their foreign investment and global value chains, can influence the social and environmental practices of businesses worldwide.”¹¹

While there appears to be a general consensus in the United States and abroad that favors international standards governing corporate business practices, attempts to reach an agreement on specific standards have proven to be less promising. In some cases, these efforts have fostered competition among countries for investment projects, have highlighted the remaining differences in national policies regarding foreign investment, and have created differences in the goals and objectives of negotiations between the developed and the developing nations. Most developed economies favor international rules, or codes of conduct, that could promote a “level playing field,” or an environment in which investment decisions are based solely on competitive market factors. Developing economies, however, often view such efforts as attempts by the developed countries to promote rules and codes of conduct that effectively allow them to hoard foreign investments for themselves and to deny the developing countries the means to compete internationally for new investment projects.

These and other differences have spurred nations and international organizations to adopt various approaches in order to promote international rules on foreign investment. One approach has been to negotiate legally binding agreements, whether they are narrowly or broadly cast, that impose a set of standards on multinational firms and that bring a large number of countries into compliance simultaneously. For example, after the United States adopted the FCPA, it supported efforts within the OECD to adopt the Convention on Combatting Bribery of Foreign Public Officials in International Business Transactions (Convention on Bribery), which focuses on a narrow set of issues related to bribing public officials.¹² Since the convention entered into force on February 15, 1999, 40 countries¹³, including the United States,¹⁴ have passed national legislation implementing the convention.

A similar approach that failed to gain agreement was a comprehensive agreement on foreign investment, known as the Multilateral Agreement on Investment (MAI). The MAI was expected to be a broad, legally binding, multi-faceted agreement that would have established an international set of rules on a wide range of foreign investment issues. Support for the agreement

⁹ Although adopted informally in 1977, the Principles were incorporated as Sec. 208, Title II of the Comprehensive Anti-Apartheid Act of 1986 (P.L. 99-440, October 2, 1986) as amended.

¹⁰ CRS Report RL30079, *Foreign Corrupt Practices Act*, by Michael V. Seitzinger.

¹¹ *World Investment Report 2011*, United Nations Conference on Trade and Development, 2011, p. 111.

¹² See <http://www.oecd.org/daf/anti-bribery/anti-briberyconvention/38028044.pdf>.

¹³ See <http://www.oecd.org/daf/anti-bribery/antibriberyconventionratification.pdf>.

¹⁴ P.L. 105-366, November 10, 1998.

eroded over the course of the negotiations, which focused on provisions that proved to be too divisive to resolve. In addition, citizen and consumer groups opposed the proposed agreement, in part because they viewed it as too favorable to multinational corporations, and because of their concerns regarding what they believed would be the social, economic, and political impact of the agreement.¹⁵

In lieu of negotiating comprehensive multilateral agreements, many countries have resorted to adopting narrowly focused bilateral investment treaties that contain codes of conduct. Often, these codes resemble a general set of investment-related provisions and corporate “best practices,” rather than a legally binding agreement. According to the United Nations, by year-end 2011, 174 countries had concluded 3,164 investment treaties and 2,833 bilateral investment treaties (ITs). Bilateral agreements dominate the number of new and existing investment agreements, but regional agreements are becoming more significant in terms of economic impact.¹⁶ Often these treaties are accompanied by some form of codes of conduct that are negotiated to cover a particular investment project or sector and tend to be highly specific to a company, project, or location.

Other Agreements

Some nations have used other types of multilateral treaties to promote codes of conduct for multinational firms. One type of agreement attempts to bring greater conformity in the treatment of foreign investment by prescribing changes in national laws governing foreign investment as one component of a broader arrangement that is geared toward economic cooperation and integration, such as the treaties that established the European Community and the North American Free Trade Agreement. There are other, legally non-binding, arrangements which cover foreign investment, the most prominent of which are: the OECD Guidelines for Multinational Enterprises;¹⁷ the OECD Principles of Corporate Governance;¹⁸ OECD Guidelines on Corporate Governance of State-Owned Enterprises;¹⁹ Code of Liberalization of Capital Movements (covering both long- and short-term capital movements);²⁰ and the Code of Liberalization of Current Invisible Operations (covering cross-border trade in services).²¹ The OECD Guidelines comprise a set of voluntary recommendations in all the major areas of corporate citizenship, including employment and industrial relations, human rights, environment, information disclosure, combating bribery, consumer interests, science and technology, competition, and taxation. The 2011 update of the Guidelines included new recommendations on human rights and corporate responsibility for their supply chains, the first such agreement in this area.²²

¹⁵ For additional information, see CRS Report 98-569, *The Multilateral Agreement on Investment: A Brief Analysis of the Current Status*, by James K. Jackson.

¹⁶ *World Investment Report*, 2012, p. xx.

¹⁷ <http://www.oecd.org/daf/inv/mne/48004323.pdf>.

¹⁸ <http://www.oecd.org/daf/ca/corporategovernanceprinciples/31557724.pdf>.

¹⁹ <http://www.oecd.org/daf/ca/corporategovernanceofstate-ownedenterprises/34803211.pdf>.

²⁰ http://www.oecd.org/daf/inv/investment-policy/capital%20movements_web%20english.pdf.

²¹ http://www.oecd.org/daf/fin/private-pensions/invisible%20operations_web%20english.pdf.

²² *Promoting Standards for Responsible Investments in Value Chins*, p. 6.

In addition, the OECD has issued a basic statement on foreign investment, The Declaration on International Investment and Multinational Enterprises,²³ which is a general statement of policy regarding the rights and responsibilities of foreign investors. The World Trade Organization (WTO) also supports the concept of a common set of rules on international corporate investment. In addition, the International Labor Organization's (ILO) Tripartite Declaration of Principles Concerning Multinational Enterprises and Social Policy provides detailed guidance on the ways firms, both domestic and foreign, can maximize their contribution to economic and social development and minimize any negative effects.²⁴

The United Nations lists ten major principles that are recognized by international declarations and agreements that have been developed by the three main organizations, the UN, the ILO, and the OECD. These main principles comprise the UN Global Compact which covers four main areas: human rights; labor standards; environment; and anti-corruption. The ten principles of the UN Global Compact are:

1. Businesses should support and respect the protection of internationally proclaimed human rights.
2. Businesses should make sure that they are not complicit in human rights abuses.
3. Businesses should uphold the freedom of association and the effective recognition of the right to collective bargaining.
4. Businesses should uphold the elimination of all forms of forced and compulsory labor.
5. Businesses should uphold the effective abolition of child labor.
6. Businesses should uphold the elimination of discrimination in respect of employment and occupation.
7. Businesses should support a precautionary approach to environmental challenges.
8. Businesses should undertake initiatives to promote greater environmental responsibility.
9. Businesses should encourage the development and diffusion of environmentally friendly techniques.
10. Businesses should work against corruption in all its terms, including extortion and bribery.²⁵

As part of the 1994 Uruguay Round on multilateral trade negotiations, the WTO adopted the agreement on Trade-Related Investment Measures (TRIMs), which recognized that certain investment measures restrict and distort trade; required signatory countries to apply national treatment; and required countries to provide a framework for reducing restrictions on foreign investment. In 1996, the WTO established a working group on investment, which has been studying the issue of investment rules, including technical regulations and standards that govern trade and investment. The Doha Declaration set out the goal of addressing foreign investment

²³ <http://www.oecd.org/daf/inv/investment-policy/oecddeclarationoninternationalinvestmentandmultinationalenterprises.htm>.

²⁴ http://www.ilo.org/wcmsp5/groups/public/@ed_emp/@emp_ent/documents/publication/wcms_101234.pdf.

²⁵ *World Investment Report, 2011*, p. 112.

issues following the conclusion of the Fifth Ministerial in Cancun in September 2003. So far, these efforts have not succeeded in achieving the stated goal of developing a “multilateral framework to secure transparent, stable and predictable conditions for long-term cross-border investment, particularly foreign direct investment.”²⁶

G-20 Investment Measures

During the early stages of the 2008-2009 financial crisis, national leaders, generally political heads of state, met as the Group of Twenty, or G-20,²⁷ to address the crisis and to develop a reform agenda. As part of that agenda, the leaders committed to keeping markets open and liberalizing trade and investment. In addition, the G-20 leaders tasked the World Trade Organization (WTO), the Organization for Economic Cooperation and Development (OECD) and the United Nations Council on Trade and Development (UNCTAD) to monitor developments and report to the G-20 on a semi-annual basis on the progress in maintaining open markets.²⁸ At the G-20 meeting in Los Cabos, Mexico on June 19, 2012, the G-20 leaders indicated that they had grown “concerned about rising instances of protectionism around the world,” and that they viewed regional and global “value chains” as relevant to world trade and that recognized “their role in fostering economic growth, employment and development” and the need to enhance the participation of developing countries in value chains.²⁹ The latest joint OECD-UNCTAD report on investment measures concluded that G-20 members “have continued to honor their pledge not to introduce restrictive measures. Nevertheless, the report warned that, “Despite this encouraging finding, persistent high unemployment, turbulence in financial markets and a weak economic recovery put intense pressure on governments to grant assistance to individual domestic companies and to preserve jobs. As a result, governments may resort to policies or practices that discriminate against foreign investors or discourage outward investment.”³⁰

Corporate and Industry-Specific Codes of Conduct

A broad range of factors are influencing firms to adopt codes of conduct. Some firms see it as enlightened self-interest, while others see it as a necessary part of risk management.³¹ Corporate codes of conduct and industry-specific codes now exist in one form or another among most large

²⁶ http://www.wto.org/english/thewto_e/minist_e/min01_e/mindecl_e.htm#tradeinvestment.

²⁷ The Group of Twenty, or G-20, is an informal forum for advancing international economic cooperation among 20 major advanced and emerging-market countries, consisting of the following members: Argentina, Australia, Brazil, Canada, China, France, Germany, India, Indonesia, Italy, Japan, Mexico, Russia, Saudi Arabia, South Africa, South Korea, Turkey, the United Kingdom, the United States, and the European Union. The G-20 was originally established in 1999 to facilitate discussions among G-20 finance ministers. The prominence of the G-20 increased with the onset of the global financial crisis in the fall of 2008, and the G-20 started meeting at the leader level, generally the political head of state. In September 2009, the G-20 leaders announced that, henceforth, the G-20 would be the “premier” forum for international economic cooperation. In its current form, the G-20 leaders meet annually, while finance ministers and central bank presidents meet in the spring and the fall prior to the annual leaders’ meeting. On-going work of the G-20 is conducted by representatives of the national leaders, referred to as Sherpas. Russia assumed the Presidency of the G-20 on December 1, 2012, and will host the next meeting of G-20 leaders on September 5-6, 2013 in St. Petersburg.

²⁸ *The G-20 Seoul Summit Leaders’ Statement*, November 11-12, 2010

²⁹ *The G-20 Los Cabos Summit Leaders’ Statement*, June 19, 2012.

³⁰ *Eighth Report on G-20 Measures*, Organization for Economic Cooperation and Development and the United Nations Council on Trade and Development, October 31, 2012, p. 4.

³¹ A Stitch in Time, *The Economist*, Special Report on Corporate Social Responsibility, January 19, 2008, p. 12.

multinational corporations and among most of the developed countries. A recent study by the OECD concluded that most corporate codes tend to be highly specific and to deal with the idiosyncrasies of a particular company, project, or location.³² Industry-specific corporate codes dealing with environment and labor issues appear to be the most common, and most U.S. manufacturers and retailers in the apparel industry have adopted corporate codes that prohibit using child, sweatshop, or prison labor. U.S. companies in such diverse industries as footwear, personal care products, photographic equipment and supplies, stationary products, hardware products, restaurants, and electronics and computers have adopted corporate codes of conduct.

Multinational corporations generally support the concept of codes of conduct that standardize rules of corporate behavior across a broad range of countries and industries. While the motivation behind adopting corporate codes of conduct can be quite complex, multinational firms generally adopt codes of conduct because they believe they represent good business practices. Generally, multinational corporations desire national treatment as a basis for any investment agreement, but are concerned that standards negotiated in one agreement could be applied to their worldwide operations, regardless of the disparity in economic conditions between locations, local customs, jurisprudence, or differences in local business practices. Some firms also argue that codes which allow foreign groups to submit complaints to U.S. regulatory bodies concerning the overseas operations of the subsidiaries of U.S. firms could be used as a competitive tool to damage the worldwide reputations of U.S. firms.

Industry-specific codes of conduct are as varied and as extensive as the multitude of industries they cover. Labor and environmental issues, however, are the two most frequently covered areas in the codes, regardless of industry. Environmental standards often comprise commitments from firms to be open to the concerns of the communities in which they locate. The most common labor codes include commitments for firms to provide a reasonable working environment, provisions against discrimination and a commitment to obey laws regarding child labor and compensation. Concerns over child and sweatshop labor, in particular, have spurred some public groups to take action on their own. The Workers' Rights Coalition,³³ an alliance of 67 universities and colleges, pressured Nike and Reebok to investigate allegations of sweatshop labor conditions in a Mexican apparel factory.

Concerns of Stakeholders

While traditional economic theory holds that corporations strive to maximize their profits to benefit the stockholders, a broad group of "stakeholders" is pressing to have their interests represented as well. These stakeholders argue that corporations have responsibilities beyond the narrow scope of their legal charters, or that they should abide by a "social contract" that reflects society's changing social and cultural mores. The size of the group of stakeholders and the social responsibilities they expect varies with the size of the firm, the industrial sector it is involved in, and its products and operations. This group of stakeholders and the associated social responsibilities also become vastly larger for firms that operate in more than one country and can include issues beyond the common areas of workers' rights, environmental concerns, and business production or financing operations. At times, the issues sought by stakeholders in one

³² Gordon, Kathryn, and Maiko Miyake. *Deciphering Codes of Corporate Conduct: A Review of Their Contents*, *OECD Working Papers on International Investment*, Number 992. OECD, October 1999. pp. 5-7.

³³ For additional information see the organization's website, <http://www.workersrights.org/>.

country can clash with those sought by stakeholders in another country, for instance when workers in developed countries push for job security, health care and other benefits, and environmental issues, while workers in developing countries push for more local jobs and local managers, worker training and education, technology transfers, and higher levels of local production.

Issues for Congress

Governments, corporations, and the public generally support the concept of corporate codes of conduct. The complexity of the issue and the diversity of foreign investments, however, make it difficult in practice to negotiate international agreements with legally binding codes of conduct and likely will present Congress with at least two large, competing groups of interests. These groups basically represent the difference between economic efficiency as represented by corporations and equity, or social justice, as represented by a broad coalition of social and public groups. Generally, economic analysis indicates that legally binding codes of conduct that eliminate market-distorting activities promote market efficiency and, thereby, provide positive net benefits to consumers and to the economy as a whole. In most cases, however, there is a mismatch between those who benefit from greater market efficiency and those who bear the costs of economic adjustment. As a result, those who bear the highest costs are likely to be the most vocally opposed and to voice that opposition to Congress, whereas those who benefit are less likely to be motivated to express their support due to the perceived limited value of the benefits.

There is no clear-cut method for determining the most equitable distribution within the economy of the costs and benefits associated with international investment. A broad coalition of public and social groups increasingly have come to view negatively the global spread of economic activity and to argue that voluntary corporate codes of conduct accomplish little. Beyond a narrow set of issues, there is less agreement on how Congress should proceed. Numerous labor and environment-related measures that garner support within the United States are opposed abroad, often by the very countries and groups the measures are intended to help. Moreover, consumer and labor groups have grown uneasy about their own economic well-being as a result of the recent slow-down in the rate of growth of the U.S. economy. As a result, they are arguing for including labor and environmental provisions in free trade agreements that are under consideration, and they may well urge Congress to adopt more restrictive measures concerning the labor and environmental impact associated with imports and foreign investment as a means of protecting domestic U.S. jobs.

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