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National Regulation of Multinational Enterprises: An Essay on Comity, Extraterritoriality, and Harmonization

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Articles

National Regulation of Multinational Enterprises: An Essay on Comity, Extraterritoriality, and Harmonization

REUVEN S. AVI-YONAH*

Despite the economic importance of multinational enterprises ("MNEs"), there is a surprising paucity of law governing foreign direct investment ("FDI"), especially in comparison with the abundance of law governing trade. There is no multilateral legal arrangement governing FDI that is similar to the General Agreement on Tariffs and Trade ("GATT"), no organization similar to the World Trade Organization, and almost no courses in law schools on FDI law. The goal of this Article is to begin to remedy this state of affairs by proposing a conceptual model for analyzing the application of the national laws of home and host countries to MNEs operating within their territories. This Article also seeks to explain the extraordinary difficulties in reaching consensus on a multilateral agreement on investment similar in scope to the GATT, and to suggest an approach to negotiating such an agreement in a new multilateral forum, the World Investment Organization.

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I. INTRODUCTION

Multinational enterprises (“MNEs”) play a major role in the world economy.¹ At the end of 2001, the gross product of all foreign affiliates of MNEs was estimated at \$3.5 trillion, or roughly one tenth of the world’s gross domestic product.² Sales by foreign affiliates of MNEs, a broad measure of the revenues generated by international production, reached an estimated \$19 trillion in 2001.³ By comparison, world exports in 2001 totaled less than \$7.5 trillion.⁴

1. The choice of terminology in this field is inevitably value-laden. MNEs is the preferred term of the rich countries and the OECD; developing countries and the U.N. prefer to call them transnational corporations (TNCs). I use MNEs not out of political preference but because TNCs is misleading in regard to the legal structure of MNEs (they are typically not one corporation), which is important for purposes of this Article.

2. UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT (“UNCTAD”), WORLD INVESTMENT REPORT 2002: TRANSNATIONAL CORPORATIONS AND EXPORT COMPETITIVENESS 4, U.N. Doc. UNCTAD/WIR/2002 (2002) [hereinafter WORLD INVESTMENT REPORT 2002]. Gross product is defined as the total value of all goods and services produced by MNEs.

3. *Id.* Sales by foreign affiliates is defined as the total value of sales by affiliates of the MNE outside its country of incorporation to unrelated parties.

4. *Id.*

About two-thirds of world trade is conducted by MNEs, and about a third takes place within MNEs.⁵ MNEs are also responsible for about 75% to 80% of global research and development activities and up to 90% of inter-country technology flows.⁶

Despite the economic importance of MNEs, there is a surprising paucity of law governing foreign direct investment ("FDI"), especially in comparison with the abundance of law governing trade.⁷ There is no multilateral legal arrangement governing FDI that is similar to the General Agreement on Tariffs and Trade ("GATT"), no organization similar to the World Trade Organization ("WTO"), and almost no courses in law schools on FDI law.⁸ The goal of this Article is to begin to remedy this state of affairs by proposing a conceptual model for analyzing the application of the national laws of home and host countries to MNEs operating within their territories.⁹ This Article also seeks to explain the extraordinary difficulties in reaching agreement on a multilateral agreement on investment ("MAI") similar in scope to the GATT, and to suggest a possible approach to negotiating such an agreement in a new multilateral forum, the World Investment Organization ("WIO").

This Article is divided into five parts. Part II lays out a conceptual model or matrix for analyzing the application of national laws to MNEs. This matrix answers the following questions: When should a legislator in a home or host country employ the "enterprise approach" by applying a national law to MNEs operating in her country on an extraterritorial basis? When, on the other hand, should she employ the "entity approach" by applying the law only to the part of the MNE within her country's territory?¹⁰

5. *Id.* at 4–5.

6. MNEs are the largest source of external finance for developing countries, so they are particularly important to those countries. *Id.* at 49–68, 73–84.

7. FDI is defined as the direct ownership of assets or over 10% in the equity of subsidiaries in another country. At the end of 1999, the stock of FDI stood at \$5 trillion. *Id.* at 4. The ownership of FDI is highly concentrated: a mere 100 parent firms, based mainly in developed countries, account for roughly one-eighth of the total assets of all foreign affiliates of MNEs. *Id.* at 8.

8. There were nearly 2,000 bilateral investment treaties at the end of 1999, but these are rarely discussed in the legal literature. *Id.* at 8. An on-line LexisNexis "US & Canadian Law Reviews, Combined" database search conducted on September 24, 2003 produced only 11 results for "bilateral investment treaty" appearing in the title, compared to 209 for "GATT" and 362 for "WTO."

9. The home country of an MNE is the country in which its parent corporation is incorporated (where the MNE has its headquarters). All other countries in which the MNE operates are called host countries.

10. The entity approach involves applying the laws of each country in which the MNE operates only to the part of the MNE that is located within its borders.

Parts III through VI of this Article then apply the model developed in Part II to specific areas of law. Part III discusses applications in which the entity approach is preferable, with occasional deviations on the basis of comity. The examples are drawn from areas of private law such as contracts and torts. Parts IV and V discuss applications in which the enterprise approach is preferable. Part IV discusses applications in which the preferred approach is the extraterritorial extension of a country's laws to the MNE on a unilateral basis. Examples are drawn from criminal law (e.g., corruption), labor law, bankruptcy, and tax. Part V analyzes situations in which the preferred approach is harmonization of the relevant laws in an appropriate international forum. Examples are taken from constitutional law (e.g., anti-discrimination), antitrust, and trading with the enemy laws. Finally, Part VI concludes by recommending the establishment of a WIO to facilitate discussion of the areas in which harmonization is the preferred approach.

II. THE MATRIX

Suppose a member of the U.S. Congress is drafting legislation that applies to MNEs. The question arises whether the proposed bill should apply to the operations of the MNE outside the territorial limits of the United States.¹¹ How should the member of Congress decide this question?

The issue of extraterritoriality as applied to MNEs involves the choice between two approaches, which Philip Blumberg has named the entity and the enterprise approaches.¹² Under the entity approach, each country in which a MNE operates applies its own law solely to the unit or units of the MNE doing business within the country's territory. If the MNE is organized in the standard way with a parent corporation in the home country and subsidiaries in the host country, the entity approach requires each country to apply its law to the corporation(s) incorporated under its laws and to no other. The

11. The Supreme Court has held that, for U.S. legislation to have extraterritorial application, Congress must state so explicitly. *EEOC v. Arab Am. Oil Co.*, 499 U.S. 244, 248 (1991). Interestingly, ARAMCO operated in Saudi Arabia through a branch, and not through a subsidiary, so the issue did not involve applying the law (Title VII) to a foreign corporation. *But see* *Hartford Fire Ins. Co. v. Cal.*, 509 U.S. 764, 813–14 (1993) (challenging the presumption in *EEOC v. Arab Am. Oil Co.*).

12. PHILIP I. BLUMBERG, *THE MULTINATIONAL CHALLENGE TO CORPORATION LAW* 63 (1993) [hereinafter *BLUMBERG, MULTINATIONAL CHALLENGE*]; Philip Blumberg, *The Increasing Recognition of Enterprise Principles in Determining Parent and Subsidiary Corporation Liabilities*, 28 *CONN. L. REV.* 295, 295–96 (1996).

entity approach is the standard or default rule in international law and the preferred approach of most commentators.¹³

The alternative is the enterprise approach, under which a single rule of law applies to the entire MNE. The enterprise approach can be implemented in two ways. One possibility is extraterritoriality, in which a single country, usually the home country, applies its laws to the entire MNE. The other possibility is harmonization, in which the various countries in which the MNE operates agree on a single harmonized set of rules to govern the MNE. A minority of commentators, most prominently Blumberg, prefer the enterprise approach.¹⁴

The choice between entity and enterprise approaches is related to another debated issue: whether MNEs have nationality—i.e., whether they can be identified as belonging primarily to a single jurisdiction, the home country. Before the 1980s, it was common to assume that MNEs were identified with their home countries and that, for example, “what is good for GM is good for America.”¹⁵ Commentators from both the right and left have recently questioned this assumption, arguing that MNEs are profit-maximizing enterprises with no particular national allegiance.¹⁶ Such commentators point out that the sources of capital, business operations (research and development, production, and distribution), employees, and customers of MNEs are increasingly global, rather than concentrated in any particular country. Others disagree, citing the fact that both management and key business operations are still located in the home country.¹⁷ The first view, which holds that MNEs lack nationality, fits more naturally with the entity approach, although an enterprise approach based on harmonization is also possible. The second view, which holds that MNEs have nationality, fits with an enterprise approach based on extraterritorial application of the home country’s

13. See RESTATEMENT (THIRD) OF THE FOREIGN RELATIONS LAW OF THE U.S. §§ 213, 414, 414 cmts. b, c (1987); EDWARD M. GRAHAM, GLOBAL INDUSTRIES AND NATIONAL GOVERNMENTS 69–100 (1996).

14. BLUMBERG, MULTINATIONAL CHALLENGE, *supra* note 12, at 168–200; PETER MUCHLINSKI, MULTINATIONAL ENTERPRISES AND THE LAW (1995); RAYMOND VERNON, IN THE HURRICANE’S EYE: THE TROUBLED PROSPECTS OF MULTINATIONAL ENTERPRISES (1998).

15. See, e.g., Raymond Vernon, *The Multinational Enterprise: Power Versus Sovereignty*, 49 FOREIGN AFF. 736 (1971); JEAN-JACQUES SERVAN SCHREIBER, THE AMERICAN CHALLENGE 3–30, 153–56 (1968); Osvaldo Sunkel, *Big Business and Dependencia: A Latin American View*, 50 FOREIGN AFF. 517 (1972).

16. See Robert B. Reich, *Who Is Us?*, 68 HARV. BUS. REV. 53 (1990); EDWARD M. GRAHAM & PAUL R. KRUGMAN, FOREIGN DIRECT INVESTMENT IN THE UNITED STATES 57–84 (3d ed. 1995).

17. Laura Tyson, *They Are Not Us*, THE AM. PROSPECT, Winter 1991, at 37.

laws.

Neither Blumberg nor other commentators have offered a conceptual model for answering the question of how to choose between these three approaches: the entity approach, harmonization, and unilateral extraterritoriality.¹⁸ Therefore, they are not helpful in resolving the dilemma faced by our legislator. This Part will attempt to outline such a conceptual framework by using a matrix.

There are two distinct issues that are relevant to answering the extraterritoriality question. The first is goal-oriented: To what extent does the purpose of the legislation require its extraterritorial application to the entire MNE? The second is practical: To what extent will the legislation, if applied on an enterprise-wide basis, conflict with the policies of other jurisdictions and/or with the preferences of the MNE itself?¹⁹ These two issues can be drawn as two axes of a matrix: a horizontal axis (X) and a vertical axis (Y).

The horizontal axis (X) can be divided into three segments. The first segment involves laws that usually have only local relevance so that their purpose generally does not require extraterritorial application. An example is speed limits on the highway: There is no reason why they should apply uniformly to an entire MNE, or even beyond a particular stretch of highway, because the purpose is to make all vehicles on that stretch of road obey the same rule. The second segment involves laws that achieve part of their purpose by being applied within a country, but that ideally would apply extraterritorially as well. Most criminal laws as well as laws having some moral dimension fall into this category. For example, child labor laws achieve some of their purpose if they protect children in one country from exploitation, but in an ideal world, all children would be protected. The third segment involves laws that do not achieve any of their purposes unless they are applied extraterritorially. A classic example, discussed below, is trading with the enemy legislation because its purpose can be completely defeated (as history shows) if subsidiaries are permitted to trade. Many economic laws, such as antitrust, bankruptcy, and tax, fall into this category as well.

18. For other approaches to a similar question, see Andrew T. Guzman, *Choice of Law: New Foundations*, 90 GEO. L.J. 883 (2002); Joel Trachtman, *Economic Analysis of Prescriptive Jurisdiction*, 42 VA. J. INT'L L. 1 (2001).

19. While the preferences of other countries are likely to be accorded some weight in any conflict of laws analysis, it may surprise the reader that I accord any weight to the preferences of the MNEs themselves. See Lea Brilmayer, *Rights, Fairness, and Choice of Law*, 98 YALE L.J. 1277 (1989). But an extensive history has shown that progress on many issues related to MNEs depends crucially on the degree to which the MNEs themselves were interested in advocating an enterprise approach. For a discussion of corruption and tax, see *infra* Part IV.A-C.

The vertical axis (Y) of the matrix can also be divided into three segments. In the first segment the policies of other jurisdictions conflict with the policies underlying the law in question. Such conflict can be expressed either in specific, conflicting legislation or in other ways, such as diplomatic protests.²⁰ For example, other countries may not share the foreign policy goals embodied in trading with the enemy legislation. In the second segment the policies of other jurisdictions are in basic agreement with the policy of the law at issue, but the MNEs themselves do not wish for the law to be applied throughout the enterprise. Tax law is a classic example: Countries are in general agreement that the profits of MNEs should only be taxed once, but the MNEs, while seeking to prevent double taxation, do not object to double non-taxation. Finally, the third segment of the vertical axis is comprised of issues on which both countries and MNEs are in general agreement. Both countries and MNEs, for example, agree that bribery of their officials should be discouraged, whatever the private view of the officials in question.²¹

The matrix appears as follows:

Y Axis				
	Countries and MNEs agree			
	Countries agree but MNEs do not			
Countries disagree				
	Law does not require extraterritoriality	Law partially requires extraterritoriality	Law requires extraterritoriality	X Axis

20. This view of policy conflict is not limited to what Currie terms “true conflict”—i.e., when it is not possible to obey both laws simultaneously. Rather, the issue is whether there is a divergence in fundamental policies of the countries in question, as expressed both in their laws and by other means. BRAINERD CURRIE, *SELECTED ESSAYS ON CONFLICT OF LAWS* 177–87 (1963).

21. It is also possible to envisage situations in which the MNEs agree but the countries do not. Such may be the case, for example, in the gender discrimination area, in which the MNEs may prefer to expand their pool of human capital by hiring more women even if the host countries disapprove. But I have not included such a fourth row because I believe that if the countries disagree, harmonization is the best option, even if the MNEs agree. The agreement by MNEs has significant implications for the prospect for harmonization.

The decision of our legislator can now be seen as depending on where the particular legal issue she faces falls within the above matrix. In general, if the law falls within the first column on the horizontal axis, the law should not be applied extraterritorially, i.e., the entity approach is preferred. If the law falls within the second and third columns of the horizontal axis, the choice of whether to apply it extraterritorially depends on its position on the vertical axis. If the legal issue falls within one of the top two rows of the vertical axis, the law should be applied extraterritorially. If the legal issue is in the bottom row on the vertical axis, the law should not be applied extraterritorially, but efforts at achieving a harmonized solution should be given high priority.

The above analysis is summarized on the matrix below:

<i>Y Axis</i>				<i>X Axis</i>
	Comity	Extraterritoriality	Extraterritoriality	
Countries and MNEs agree	Comity	Extraterritoriality	Extraterritoriality	
Countries agree but MNEs do not	Comity	Extraterritoriality	Extraterritoriality	
Countries disagree	Comity	Harmonization	Harmonization	
	Law does not require extraterritoriality	Law partially requires extraterritoriality	Law requires extraterritoriality	

Comity refers to a situation in which a country's laws do not normally apply extraterritorially (the entity approach is preferred), but can be applied extraterritorially by courts on a case-by-case basis. Examples of this outcome from private law (torts and contracts) are described in Part III. Extraterritoriality refers to the unilateral extraterritorial application of the home country's law to a MNE whose parent is incorporated in that country. In most situations, host countries may then refrain from applying their law to those MNEs so that each MNE is governed entirely by the law of the home country. This approach is labeled extraterritoriality with reciprocity.²²

22. Countries may object to having the law of another country apply within their territory as a matter of sovereignty, even if they agree with the policy of the law in question. But in today's world, some measure of extraterritorial application of laws is inevitable. See Larry Kramer, *Vestiges of Beale: Extraterritorial Application of American Law*, 1991 SUP.

Examples from various areas of law, such as corruption, bankruptcy, tax, and child labor, are described in Part IV. Harmonization refers to situations in which the law should not be applied extraterritorially on a unilateral basis, but efforts should be made to achieve a harmonized solution. Part V describes examples of this approach, such as trading with the enemy, discrimination, and antitrust. Part VI proposes the establishment of a WIO to provide a forum for such negotiations.

III. COMITY

The examples in this Part are drawn from two areas of private law: torts and contracts. In general, private law may tend to fall within the first column of the horizontal axis—i.e., the law does not require extraterritoriality because it deals primarily with local issues, such as the protection of property rights in a jurisdiction or damages for a tort occurring in the jurisdiction. Cross-border contracts may be seen as an exception, but even they can usually be dealt with locally since they typically involve a choice of law provision either explicitly or by default.

A. *Torts: The Bhopal Case*

On the night of December 2, 1984, a deadly gas (methyl isocyanate) was released from a chemical plant operated in Bhopal, India by Union Carbide India Limited (“UCIL”), a 51% owned subsidiary of the Union Carbide Corporation (“UCC”), a Delaware corporation. The result was the most devastating industrial disaster in history—the death of over 2,000 persons and injuries to over 200,000. Four days later, the first of 145 class actions against UCC was commenced in federal district court. The cases were consolidated before Judge John F. Keenan of the Southern District of New York. Judge Keenan eventually dismissed the actions with certain conditions, and the dismissal was upheld on appeal. The most important condition was that UCC agree to submit to the jurisdiction of Indian courts. Ultimately, UCC settled the Indian cases for about \$850 million, which was disbursed to the victims after long delays.²³

On its face, the decision in the Bhopal case involved a

CT. REV. 179 (1991). In addition, the fact that extraterritoriality is applied only to MNEs and that reciprocity is available may help to assuage sovereignty concerns.

23. *In re Union Carbide Corp. Gas Plant Disaster*, 809 F.2d 195 (2d Cir. 1987).

straightforward application of the doctrine of *forum non conveniens*. The Bhopal plant was owned and operated by UCIL, an Indian corporation, 49% of which was owned by Indians. Although the plant was originally designed by UCC, the design was changed many times during the ten years of construction. No Americans were employed at the plant, and none had visited it for a year prior to the accident. The accident had occurred in India, the victims were all Indians, and the witnesses were mostly Indian.²⁴

However, one major hurdle blocked the transferring of the case to Indian courts: Under generally accepted principles of international law, Indian courts would not have jurisdiction over UCC because it had no connection with India other than its ownership of stock in UCIL. If recovery were limited to the assets of UCIL, then it only would have consisted of the defunct Bhopal plant. Therefore, the Union of India, which acted on behalf of the victims, sought from the beginning to extend jurisdiction to UCC on an extraterritorial basis (host country extraterritoriality). Judge Keenan agreed, conditioning his dismissal of the action on UCC's agreement to submit to the jurisdiction of the Indian courts, a condition that was upheld on appeal.²⁵ As a result, the case was settled by UCC in India.

The question of whether limited liability should protect shareowners from tort liabilities resulting from corporate activity has been debated extensively.²⁶ Whatever view one takes on this issue, some of the problems, such as determining who the shareholders are and apportioning the liability, disappear in the context of a MNE.²⁷ But other issues remain. In particular, commentators have disagreed on whether the internalization of the harm caused by the corporation

24. *Id.* at 200–01. Ironically, both the minority ownership and the all-Indian operation of the plant were “performance requirements” imposed by the Indian government as a condition for agreeing to allow UCC to invest in India. Such requirements are frequently imposed by developing countries seeking to force MNEs to transfer technology to them, since technology transfer is generally considered the aspect of FDI most likely to generate vertical externalities. See Christos N. Pitelis & Roger Sugden, *On the Theory of the Transnational Firm*, in *THE NATURE OF THE TRANSNATIONAL FIRM* 9 (Christos N. Pitelis & Roger Sugden eds., 1991); Edward K.Y. Chen, *Introduction*, in *TRANSNATIONAL CORPORATIONS AND TECHNOLOGY TRANSFER TO DEVELOPING COUNTRIES* 1 (1993) (Edward K.Y. Chen ed., 1993).

25. 809 F.2d at 203.

26. Henry Hansmann & Reinier Kraakman, *Toward Unlimited Shareholder Liability for Corporate Torts*, 100 YALE L.J. 1879 (1991); Janet Cooper Alexander, *Unlimited Shareholder Liability through a Procedural Lens*, 106 HARV. L. REV. 387 (1992).

27. Because the only shareholder of the subsidiary is the parent or another affiliate, some of the technical issues that arise for public shareholders do not apply in the MNE context. See Nina A. Mendelson, *A Control-Based Approach to Shareholder Liability for Corporate Torts*, 102 COLUM. L. REV. 1203 (2002).

and the monitoring of the subsidiary would be improved by imposing liability on its corporate parent, or whether this would excessively deter risk-taking.²⁸ In general, American courts have tended to favor the latter view. They have refused to “pierce the corporate veil” by imposing liability on corporate parents when not expressly required by statute to do so.²⁹

Whatever the merits of this debate, it is clear that current law does not require an enterprise approach to all tort cases involving subsidiaries of MNEs, although courts frequently pierce the veil in those cases because of the involuntary nature of the liability and its implications for monitoring and cost internalization.³⁰ It would therefore appear that this category of cases falls into the first column of the horizontal axis, and that comity, a case-by-case determination of whether an enterprise approach should be applied, is the preferred solution. The Bhopal case would thus represent an exception, in which the extraordinary nature of the case caused the U.S. court to approve of a remedy that effectively implemented an enterprise approach of host country extraterritoriality. It is not clear that such a remedy should be applied in all toxic tort cases.

B. *Contracts: The Deltec Litigation*

The Deltec litigation involved an Argentine corporation, Cia-Swift, that was a wholly-owned subsidiary of a Bahamas corporation, Deltec.³¹ Creditors of Cia-Swift (the largest Argentine meatpacker) sued to force it into bankruptcy reorganization. A company-appointed referee originally found that the company's assets exceeded its liabilities, even including inter-company debts. However, at the insistence of a minor creditor with a \$4,000 claim, the Argentine court extended the liabilities of Cia-Swift to the entire Deltec enterprise by relying on the “unified structure of decision and interest

28. *Id.*; BLUMBERG, MULTINATIONAL CHALLENGE, *supra* note 12, at 121–48; Joseph A. Grundfest, *The Limited Future of Unlimited Liability: A Capital Markets Perspective*, 102 YALE L.J. 387 (1992).

29. BLUMBERG, MULTINATIONAL CHALLENGE, *supra* note 12, at 121–48; Robert B. Thompson, *Piercing the Corporate Veil: An Empirical Study*, 76 CORNELL L. REV. 1036 (1991).

30. BLUMBERG, MULTINATIONAL CHALLENGE, *supra* note 12, at 190.

31. “Compania Swift de la Plata S.A.,” 146 L.L. 601 (1972), *translated in* Michael W. Gordon, *Argentine Jurisprudence: The Parke Davis and Deltec Cases*, 6 LAW. AM. 320 (1974); *see also* Deltec Banking Corp. v. Compania Italo Argentina de Electricidad S.A., *available at* 171 N.Y.L.J. 18, at col. 1.

which makes [the Deltec enterprise] a single unit.”³² The Argentine Supreme Court affirmed, declaring that grave national interests were at stake in the relationship between the “interdependence, linkages and multinational nature” of the MNEs, on the one hand, and the “paramount interests of [Argentine] society,” on the other.³³ The court therefore extended the liabilities to the entire Deltec group, applying the enterprise approach of host country extraterritoriality.³⁴

The Deltec decision evoked “severe international hostility.”³⁵ A New York court declared that:

There is little doubt that the finding of Bankruptcy in Argentina is not in conformity with American Statutory or decisional law The determination that plaintiff is Bankrupt because it is one segment of a chain of corporations, one of which is insolvent, may under our laws amount under certain circumstances to a confiscation of property.³⁶

The court therefore refused to follow that judgment, and it was affirmed on appeal.³⁷

The application of enterprise principles is more questionable here than in the Bhopal case because the Argentine creditors were largely voluntary—they extended credit to Cia-Swift in full awareness of limited liability laws—and could have negotiated for a guarantee from Deltec. On the other hand, some of the creditors, including the one with a claim for \$4,000, were trade creditors and therefore closer to involuntary creditors. In this case as well, the correct approach appears to be the entity approach with occasional piercing of the corporate veil, to be respected or not by other courts on the basis of comity. Argentina’s attempt to codify the result in Deltec into its law was not respected by other jurisdictions and was promptly repealed when the Peronistas lost power in 1976.³⁸

32. *Compania Swift*, 146 L.L. at 603.

33. “*Compania Swift de la Plata S.A.*,” CSJN 151 L.L. 516 (1973), *translated in* Gordon, *supra* note 31, at 337–38.

34. BLUMBERG, MULTINATIONAL CHALLENGE, *supra* note 12, at 188.

35. *Id.* at 189.

36. *Deltec Banking Corp.*, 171 N.Y.L.J. at 18.

37. *Deltec Banking Corp. v. Compania Italo Argentina de Electricidad S.A.*, 362 N.Y.S.2d 391 (1974).

38. BLUMBERG, MULTINATIONAL CHALLENGE, *supra* note 12, at 189.

IV. EXTRATERRITORIALITY

The examples in this Part illustrate situations in which the purpose of the law fully or partially requires extraterritorial application, and in which the other jurisdictions involved agree in principle with the underlying purposes of the law in question, even though they may not agree with many of the detailed rules. In these circumstances, the unilateral application of the law on an extraterritorial basis to the entire MNE is justified. The home country would usually be the one applying its law to the entire MNE. The other countries would either cede jurisdiction or apply their own law concurrently within their territory.

This Part will first consider examples in which the MNEs themselves agree with the underlying purpose of the law in question (the top row of the matrix), and then examples in which they disagree (the middle row of the matrix). The first type constitutes the most promising area for extraterritorial application of the law, because, in those cases, the MNEs would prefer that the law be applied extraterritorially, and the only constraint is their concern about competition with other MNEs (whose countries do not apply the law extraterritorially). However, this Part also argues that the law should be applied extraterritorially in the second type of cases as well to overcome similar “prisoners’ dilemma” situations.

A. Corruption

In 1977, the United States adopted the Foreign Corrupt Practices Act (“FCPA”).³⁹ The FCPA was the outcome of an extensive post-Watergate investigation by the U.S. Securities and Exchange Commission of bribes paid by U.S. MNEs to foreign officials, which led to the disgrace of the Prime Minister of Japan and the Prince Consort of the Netherlands.⁴⁰ The FCPA applies to U.S. corporations, citizens, and residents, as well as foreign corporations whose shares trade in the U.S. securities market. It applies specifically to foreign corrupt practices outside the United States.⁴¹

39. 15 U.S.C. § 78dd-1, 2 (1977).

40. For the history of the FCPA, see generally Alejandro Posadas, *Combating Corruption under International Law*, 10 DUKE J. COM. & INT’L L. 345 (2000). On the problem of corruption and its adverse economic effects, see generally SUSAN ROSE-ACKERMAN, *CORRUPTION AND GOVERNMENT: CAUSES, CONSEQUENCES, AND REFORM* (1999).

41. 15 U.S.C. § 78dd-1(g), 2(i).

The Act criminalizes any “offer, authorization of payment, or payment of anything of value” to certain foreign recipients including foreign government officials.⁴² The payment must be made for the purpose of influencing any act or decision of the foreign recipient in his official capacity, inducing the foreign official to act, or refrain from acting, in violation of his lawful duty, securing any improper advantage, or inducing such foreign recipient to use his influence to affect decisions of governments or instrumentalities.⁴³

The impact of this unilateral extraterritorial extension of U.S. law to primarily U.S. MNEs has been much debated. On the one hand, some scholars have argued that the FCPA reflects “cultural imperialism”: Payments considered commonplace in one culture may be considered corrupt in another.⁴⁴ This issue was addressed to some extent by a 1988 amendment to the FCPA, which clarified that it does not apply to payments that are lawful in the jurisdiction of the foreign recipient.⁴⁵ Another strand of criticism relates to the FCPA’s effectiveness. Some scholars have argued that U.S. MNEs have in fact done little to respond to the FCPA, and a recent Bribe Payers Index published by Transparency International shows that twenty-five years after the enactment of the FCPA the United States ranks an unimpressive nine out of nineteen on corporate propensity to bribe senior officials.⁴⁶ Other studies, however, have tended to show that the FCPA has been effective in curbing some foreign corrupt behaviors by U.S. MNEs.⁴⁷ In particular, U.S. MNEs certainly seem to have felt that the FCPA put them at a competitive disadvantage

42. *Id.* § 78dd-1(a)(3), 2(a)(3).

43. *Id.* § 78dd-1(a), 2(a), 3(a).

44. GEORGE C. GREANIAS & DUANE WINDSOR, *THE FOREIGN CORRUPT PRACTICES ACT* 129 (1982); Steven R. Salbu, *Transnational Bribery: The Big Questions*, 21 NW. J. INT’L L. & BUS. 435, 446, 454 (2001). But even Salbu, the most consistent critic of the FCPA, admits that some bribes are clearly unethical. *Id.* at 438–39.

45. 15 U.S.C. § 78dd-1(c)(1), 2(c)(1). The mere absence of a foreign law criminalizing the practice does not, however, remove the taint.

46. Salbu, *supra* note 44, at 452 n.85; Mary Jane Sheffett, *The Foreign Corrupt Practices Act and the Omnibus Trade and Competitiveness Act of 1988: Did They Change Corporate Behavior?*, 14 J. PUB. POL’Y & MKTG. 290 (1995).

47. JAMES R. HINES, *FORBIDDEN PAYMENT: FOREIGN BRIBERY AND AMERICAN BUSINESS AFTER 1977* (Nat’l Bureau of Econ. Research, Working Paper No. 5266, 1995); Paul J. Beck et al., *The Impact of the Foreign Corrupt Practices Act on U.S. Exports*, 12(4) MANAGERIAL & DECISION ECON. 295 (1991) (stating that “the results of the study provide evidence that the FCPA had a negative effect on U.S. exports to non-Latin American countries”); Christopher Hall, *The Foreign Corrupt Practices Act: A Competitive Disadvantage, But For How Long?*, 2 TUL. J. INT’L & COMP. L. 289 (1994) (reviewing empirical studies that indicate FCPA had significant effect); Michael W. Maher, *The Impact of Regulation on Controls: Firms’ Response to the FCPA*, 56 ACCT. REV. 751 (1981) (indicating that most firms incurred expenditures to comply with FCPA).

against MNEs from other countries that lacked similar legislation (in Japan, Germany, and the United Kingdom, foreign bribes were both legal and tax-deductible).⁴⁸ Their response was at first to lobby the U.S. government to change the FCPA, which led to some modifications of the Act in 1988. Most significantly, the 1988 amendments established a “grease payment” exception, providing that the Act does not apply to payments made to foreign government officials for “routine government action.”⁴⁹ But the scope of this exception is unclear, and the core provisions of the FCPA remained unchanged.⁵⁰

The U.S. MNEs then tried a new approach under the Clinton Administration: they attempted to persuade other developed countries to adopt legislation similar to the FCPA. This approach bore fruit in 1997, when the Organisation for Economic Cooperation and Development (“OECD”), joined by five other countries, formally adopted the Convention on Combating Bribery of Foreign Public Officials in International Business Transactions, which came into force in 1999.⁵¹

The OECD Convention represents a significant achievement.⁵² OECD member countries are home to about 90% of the world’s MNEs, and the addition of countries, such as Argentina, Brazil, and Chile, raises the percentage of MNEs covered even higher. The OECD Convention includes the main provisions of the FCPA, including criminalizing foreign bribery. Article 1 of the Convention establishes the parties’ unqualified obligation, specifically:

to take such measures as may be necessary to establish that it is a criminal offence under its law for any person intentionally to offer, promise or give any undue pecuniary or other advantage, whether directly or through intermediaries, to a foreign public official, for that official or for a third party, in order that the official act or refrain from acting in relation to the

48. Hall, *supra* note 47, at 303.

49. 15 U.S.C. § 78dd-1(b), 2(b) (as amended by the Omnibus Trade and Competitiveness Act of 1988, Pub. L. No. 100-418, 102 Stat. 1107).

50. Salbu, *supra* note 44, at 449–53.

51. Convention on Combating Bribery of Foreign Public Officials in International Business Transactions, Dec. 18, 1997, 37 I.L.M. 1 (1998) [hereinafter OECD Convention].

52. For debate on the OECD Convention, see Stanley J. Marcuss & Seth Goldschlager, *An Uneven International Playing Field*, WASH. POST, Dec. 17, 1997, at A25; Stuart Eizenstat, *The Anti-Bribery Treaty*, WASH. POST, Jan. 16, 1998, at A20; Stephanie Flanders, *Clear Thinking on Corruption*, FIN. TIMES, June 23, 1997, at 10.

performance of official duties, or in order to obtain or retain business or other improper advantage⁵³

The Convention also includes the two exceptions to the FCPA: the legally allowed conduct exception and the grease payments exception.⁵⁴ In general, the intent of the Convention is to achieve “functional equivalence” of the laws of the signatory countries, while recognizing that differences in legal systems—e.g., the degree to which corporations can be made criminally liable—preclude complete identity.⁵⁵

From the perspective outlined above, corruption clearly falls within the central column of the horizontal axis: In an ideal world, bribes are illegal both domestically and overseas so that the purpose of legislation to combat bribes can best be achieved by applying it extraterritorially. On the vertical axis, bribes to domestic officials are illegal in almost every country, and the MNEs themselves would prefer not to pay them. Thus, corruption falls in the top row of the vertical axis. The only argument against applying an anti-corruption law extraterritorially is that it can place domestic MNEs at a competitive disadvantage. However, when both the countries and the MNEs agree with the underlying purpose of the law, this prisoners’ dilemma can be overcome. Although each country may be reluctant to apply its law extraterritorially for fear of disadvantaging its MNEs, if one country does so, others can be induced to follow suit. This is what happened with the FCPA and the OECD Convention, which effectively removed the competitiveness problem by applying the FCPA to most, if not all, MNEs. Thus, the corruption example is a classic case in which unilateral extraterritoriality by one country, the United States, was able to achieve some good, in part because of the incentive effect on U.S. MNEs that strenuously lobbied for the OECD Convention.

B. Bankruptcy

In the area of international bankruptcies, there has been a long-standing consensus that the correct policy outcome only can be achieved under “universalism,” i.e., an enterprise approach. Under this approach, a single court in the home country of the debtor (or in

53. OECD Convention, *supra* note 51, art. 1, 37 I.L.M. at 4.

54. *Id.* cmts. 8–9.

55. *Id.*

this case, the parent of a MNE) determines the allocation of all the assets of the debtor among all its creditors. In contrast, the prevailing legal regime in actual international bankruptcies is “territorialism,” i.e., an entity approach, where the creditors in each jurisdiction get the assets that are located in that jurisdiction when bankruptcy is declared.⁵⁶

The debate between universalism and territorialism involves precisely the type of considerations underlying the matrix described above. On the horizontal axis, there is general agreement that the universalists’ approach is better because it leads to a more rational division of the assets among creditors and reduces the transaction costs of litigating the bankruptcy in multiple fora. The debate, however, revolves around the vertical axis. Universalists like Jay Westbrook and Andrew Guzman see few areas of disagreement among countries in according priority to different claims in bankruptcy. Territorialists like Lynn LoPucki see many areas of disagreement, in particular involving priority accorded to the rights of employees.⁵⁷

Lucian Bebchuk and Andrew Guzman show that from an ex ante perspective, the interests of both countries and MNEs favor universalism. The MNEs favor universalism; since creditors adjust their lending terms to take territorialism into account, the borrowing MNE bears the cost of territorialism. Countries also favor universalism; since on average they are unlikely to gain from a territorialist approach, the welfare loss from territorialism falls on them. However, Bebchuk and Guzman also identify a prisoners’ dilemma: If other countries are universalist, it is in the interest of any given country to be territorialist because it would attract more FDI

56. See generally Andrew T. Guzman, *International Bankruptcy: In Defense of Universalism*, 98 MICH. L. REV. 2177 (2000) [hereinafter Guzman, *International Bankruptcy*]; Lynn M. LoPucki, *Cooperation in International Bankruptcy: A Post-Universalist Approach*, 84 CORNELL L. REV. 696 (1999); Lucian A. Bebchuk & Andrew T. Guzman, *An Economic Analysis of Transnational Bankruptcies*, 42 J.L. & ECON. 775 (1999). Most countries are overtly territorialist in their approach—e.g., Japan, and even countries like the United States and the United Kingdom, despite the fact that both are more open to foreign administration. See 11 U.S.C. § 304 (allowing a foreign representative to petition the bankruptcy court to turn over a U.S. debtor’s assets to the foreign creditor). When the interests of domestic creditors might be adversely affected, however, even these countries are likely to become territorialist in practice. See, e.g., *Overseas Inn v. United States*, 911 F.2d 1146 (5th Cir. 1990) (refusing to grant comity to Luxembourg court reorganization plan when it would prejudice IRS claim for unpaid taxes); Bebchuk & Guzman, *supra*; see also Robert K. Rasmussen, *Resolving Transnational Insolvencies through Private Ordering*, 98 MICH. L. REV. 2252 (2000).

57. LoPucki, *supra* note 56, at 710–11. But see Guzman, *International Bankruptcy*, *supra* note 56, at 2197–98 (arguing that in practice there is considerably more agreement in employment rather than bankruptcy statutes).

and the presumed vertical externalities.⁵⁸ Thus, all countries would defect by choosing territorialism, and the first best equilibrium will not be achieved.

On our matrix, bankruptcy thus belongs in the top right hand corner: An enterprise approach is required on the horizontal axis, and both countries and MNEs agree on the vertical axis. Therefore, home countries should unilaterally extend their bankruptcy law to MNEs whose parent is incorporated there.⁵⁹ The key issue is whether host countries will respect such extraterritorial jurisdiction, which may disadvantage their creditors. However, to the extent that host countries are also home countries, which has been true in most of the significant international bankruptcies—e.g., Maxwell, BCCI, Olympia, and Yorke—agreement should be possible through a regime of reciprocity.⁶⁰ Under reciprocity, a host country will agree to cede jurisdiction to a home country in exchange for the home country's agreement to cede jurisdiction when it is the host country.⁶¹ In practice, there has been significant progress in this area, as evidenced by the wide acceptance of the UNCITRAL Model Law on Cross-Border Insolvency.⁶² The Model Law defines the home country as the country in which the "center of main interest" of the bankrupt MNE is located, and urges courts of the host country to impose a stay and transfer assets to be divided under the jurisdiction of the home country's court. However, in a concession to territorialist countries, this procedure can be blocked by filing a separate proceeding in the

58. See Beבחuk & Guzman, *supra* note 56, at 804; see also Frederick Tung, *Is International Bankruptcy Possible?*, 23 MICH. J. INT'L L. 31, 52–69 (2001) (arguing that universalism is not feasible from a game theory perspective).

59. In some cases, it may be difficult to identify the home country. See LoPucki, *supra* note 56, at 713. In the vast majority of cases, however, this is not a problem. See Guzman, *International Bankruptcy*, *supra* note 56, at 2207. United States bankruptcy law extends to assets outside the United States, and the doctrine of substantive consolidation makes it easy to include an entire MNE. See U.N. COMM'N ON INT'L TRADE LAW, MODEL LAW ON CROSS-BORDER INSOLVENCY WITH GUIDE TO ENACTMENT, U.N. SALES NO. E.99.V.3, art. 17(2)(a) [hereinafter UNCITRAL MODEL LAW] (recognizing a foreign proceeding if it takes place in the country where the debtor's center of main interests is located).

60. See IAN F. FLETCHER, CROSS-BORDER INSOLVENCY (1990).

61. There may be substantive areas of disagreement that relate to the ultimate goal of bankruptcy law as opposed to detailed priorities, e.g., the tendency of U.S. law to favor reorganization and of U.K. law to favor liquidation. But this type of divergence affects mostly policies of home countries and thus can be resolved by agreeing that home country law will control—i.e., U.S. MNEs will be governed by U.S. law and U.K. MNEs by U.K. law.

62. The UNCITRAL Model Law was completed with input from 36 members and 40 observers of UNCITRAL. See Jay Lawrence Westbrook, *A Global Solution to Multinational Default*, 98 MICH. L. REV. 2276 (2000).

host country.⁶³

C. Tax

In the area of tax law, it is easy to show that the enterprise approach is needed on the horizontal axis. Decades of experience have shown that the entity approach to taxing MNEs—i.e., separate accounting—is not feasible and that the only viable alternative is an enterprise approach consisting of worldwide combined reporting with formulary apportionment.⁶⁴ Moreover, countries generally agree that the goal of the international tax regime should be to tax MNEs once at a rate of between 30% and 40%.⁶⁵ One problem with achieving this goal is that it is not shared by the MNEs, who prefer not to be overtaxed but also do not mind being undertaxed. Thus, tax belongs in the last column of the horizontal axis and the middle row of the vertical axis. Another problem is that even though countries agree on the need to tax MNEs at their source, tax competition drives them to refrain from doing so since they fear that they will drive FDI to other countries that grant tax holidays.⁶⁶

The solution is for home countries to tax their MNEs on an enterprise-wide basis, while granting a credit for source country taxation.⁶⁷ This will remove the incentive for source countries to engage in tax competition and enable them to levy their tax. Despite the concern about harming the competitiveness of its MNEs, the United States can adopt this rule unilaterally. Experience has shown that when the United States first adopted this rule for the passive income of its MNEs in 1962, the U.S. MNEs induced other home countries to adopt similar rules. Moreover, the experience of the OECD Convention has demonstrated that the OECD can be a good forum for resolving competitiveness concerns; in fact, the OECD is committed to expanding home country tax jurisdiction to combat

63. In practice, such proceedings may be more difficult to maintain than before the Model Law was adopted.

64. Reuven S. Avi-Yonah, *The Rise and Fall of Arm's Length: A Study in the Evolution of U.S. International Taxation*, 15 VA. TAX REV. 89 (1995).

65. Reuven S. Avi-Yonah, *The Structure of International Taxation: A Proposal for Simplification*, 74 TEX. L. REV. 1301 (1996).

66. Reuven S. Avi-Yonah, *Globalization, Tax Competition, and the Fiscal Crisis of the Welfare State*, 113 HARV. L. REV. 1573 (2000).

67. The source country is the country from which the income derives; the home or residence country is the country in which the parent of the MNE is incorporated.

harmful tax competition.⁶⁸ The remaining issue is defining the source of active income for purposes of host country taxation and foreign tax credit. The best solution is a default formula, which was recently recommended by the EU Commission for inter-EU transactions.⁶⁹

D. *Child Labor*

The problem of child labor has been one of the more contentious issues facing MNEs in the last few decades.⁷⁰ On one hand, child advocacy non-governmental organizations (“NGOs”) and some Western governments have been pushing for the “total elimination” of all forms of child labor through the International Labor Office (“ILO”) and, in some cases, the WTO. On the other hand, developing countries have generally been resistant to such moves, which they see as a disguised form of protectionism and a form of cultural imposition. MNEs have been caught in the middle, and some—e.g., Nike—have been the target of campaigns and pressure from both sides.

In the specific context of MNEs, however, the issues can be narrowed somewhat.⁷¹ First, the cultural imperialism problem is less present in this context because FDI in developing countries is less than a century old and traditional child labor practices have been followed for many centuries.⁷² Second, the most contentious issue for most developing countries is their opposition to the linkage between child labor or any labor standards and trade sanctions.⁷³ This issue is

68. See ORG. FOR ECON. CO-OPERATION & DEV., *HARMFUL TAX COMPETITION* (1998) (though admittedly covering less than full home country taxation on an enterprise-wide basis).

69. EUR. COMM’N, *COMPANY TAXATION IN THE INTERNAL MARKET* (2001) (describing formulae used in the United States at the state level and in Canada, without recommending a specific formula for the European Union).

70. See generally Christopher M. Kern, *Child Labor: The International Law and Corporate Impact*, 27 SYRACUSE J. INT’L L. & COM. 177 (2000); David M. Smolin, *Conflict and Ideology in the International Campaign Against Child Labor*, 16 HOFSTRA LAB. & EMP. L.J. 383 (1999); Kristin Weldon, *Piercing the Silence or Lulling You to Sleep: The Sounds of Child Labor*, 7 WIDENER L. SYMP. J. 227 (2001).

71. See Steven Ratner, *Corporations and Human Rights: A Theory of Legal Responsibility*, 111 YALE L.J. 443 (2001) (arguing that MNEs can be held responsible under international law for behavior that violates human rights).

72. For an argument on why the cultural imperialism question (here in the context of female genital mutilation) does not actually pose a problem for human rights abuses, see Riane Eisler, *Human Rights: Toward an Integrated Theory of Action*, 9 HUM. RTS. Q. 287, 296 (1987).

73. See Ministerial Conference of the World Trade Organization, Singapore Ministerial Declaration, adopted Dec. 13, 1996, 36 I.L.M. 218 (1997).

not directly raised in the MNE context.

Instead, one can frame the child labor issue in this context more narrowly by looking at the matrix. Child labor belongs in the middle column of the horizontal axis: Child labor laws in home countries are designed primarily to protect children in the home country, but in an ideal world, they would protect children in other countries as well.

As for the vertical axis, there has been a significant measure of agreement by countries on the goal of abolishing at least the most egregious forms of child labor. First, most countries have laws against child labor on the books, although enforcement in developing countries is sporadic. Second, almost all countries—the United States being a notorious exception—have ratified the U.N. 1989 Convention on the Rights of the Child (“CRC”).⁷⁴ The CRC includes a requirement for State Parties to protect children from hazardous and harmful employment, to ensure that employment does not interfere with a child’s education, and to establish minimum ages for employment.⁷⁵ Third, in 1998, the ILO adopted a Declaration on Fundamental Principles and Rights at Work, which binds all 174 members of the ILO to “respect, promote and realize” the principles of the seven core ILO Conventions, including the 1973 Minimum Age Convention.⁷⁶ Thus, although most ILO members have not yet ratified the 1973 Convention or the 1999 Convention on the Elimination of the Worst Forms of Child Labour, the 1998 Declaration can be seen as a statement that, in principle, they do not support child labor and would like to abolish it if they could economically afford to do so.

While the MNEs would prefer not to see home country legislation on child labor extended extraterritorially, this extraterritorial application is appropriate given the level of agreement that has been reached on this issue. Extending home country laws to MNEs operating abroad neither impinges on long-held cultural traditions nor offends deeply held host country policies favoring child labor. It also does not prevent child labor from occurring in the host country outside the MNE context—that is left to host country control,

74. Convention on the Rights of the Child, Nov. 20, 1989, G.A. Res. 44/25, U.N. GAOR, 44th Sess., Supp. No. 49, at 167, U.N. Doc. A/44/736 (1989) [hereinafter CRC]. The United States is the only major country not to have ratified the CRC (the other non-parties are Somalia and East Timor). Status of Ratification of the Principal International Human Rights Treaties, available at <http://www.unhcr.ch/pdf/report.pdf> (last visited June 19, 2003).

75. CRC, *supra* note 74, art. 32, U.N. Doc. No. A/44/736, 1989.

76. Smolin, *supra* note 70, at 420–21.

to be exercised as economic circumstances permit. It, however, does prevent MNEs from directly employing children, which sends a significant symbolic message (more than voluntary codes of conduct can achieve). While the children may work elsewhere, it also is conceivable that the higher wages earned by adults working for the MNEs may enable some of these children to go to school.

V. HARMONIZATION

This Part will consider examples in which the purpose of the legislation requires its extraterritorial application, but the countries' policies fundamentally diverge. Under these circumstances, unilateral extraterritoriality is likely to be self-defeating. Instead, the proper response is to attempt to negotiate a harmonized solution to those issues that offer some possibility of agreement, while refraining from action on the other issues. The proper forum for such negotiations will be discussed in Part V.

A. *Trading with the Enemy*

Trading with the enemy is the area in which the application of the entity or enterprise approach has been the focus of attention for the longest period. The issue first surfaced during World War I, when laws were adopted in both the United Kingdom and the United States to prohibit trading with the "enemy," defined to include enemy corporations. The issue then arose whether this legislation prohibited trading with domestic corporations controlled by enemy parents. In a decision rendered at the height of the war, the House of Lords held that if enemy control could be established, the law applied in this situation as well (the host country enterprise approach).⁷⁷ In a decision rendered well after the war was over, the U.S. Supreme Court held that the law did not apply to domestic corporations (the entity approach).⁷⁸

The futility of an entity approach to this issue soon became apparent. During World War II, the U.S. Congress amended the Trading with the Enemy Act to include all corporations directly or indirectly controlled by the enemy. Although the definition of "enemy" was not amended, the U.S. Supreme Court upheld the

77. *Daimler Co. v. Continental Tyre and Rubber Co.*, 2 A.C. 307 (H.L. 1916).

78. *Behn, Meyer & Co. v. Miller*, 266 U.S. 457, 473 (1925).

expanded application.⁷⁹ Thus, it became the established understanding that trading with the enemy legislation had to be extended on an enterprise-wide basis to be effective.⁸⁰

These early cases involved host country applications in wartime. Trouble arose, however, when the same principle was extended to home country extraterritoriality in times of peace. At the height of the Cold War in the 1950s, both U.S. MNEs and U.S. allies accepted the extraterritorial application of trading with the enemy legislation. As the Cold War alliance began to unravel during the 1960s, host countries began to object. Thus, in 1965 a French court approved a petition by the minority shareholders of Fruehauf-France, a 66% subsidiary of Fruehauf Corporation (U.S.), to appoint an administrator to carry out a contract involving sales of trucks to the People's Republic of China. The court stated that otherwise, the damages

would be of such an order as to ruin the financial equilibrium and the moral credit of Fruehauf-France, S.A., and provoke its disappearance and the unemployment of more than 600 workers [T]he judge-referee must take into account the interests of the company, rather than the personal interests of any shareholders even if they be the majority.⁸¹

By the early 1980s, the ability of the United States to extend its sanctions to U.S.-based MNEs extraterritorially was in serious jeopardy. This became clear during the Russian gas pipeline affair, in which the Reagan Administration tried to extend export control regulations to "any partnership, association, corporation, or other organization, wherever organized or doing business, that is owned or controlled by" U.S. corporations.⁸² A Dutch court held that this regulation was not binding as a matter of international law and that a Dutch wholly-owned subsidiary of a U.S. parent had to fulfill its contractual obligation to sell geophones to the former Soviet Union. The court stated that none of the established exceptions to the

79. *Clark v. Uebersee Finanz-Korporation*, 332 U.S. 480, 489–90 (1947).

80. See BLUMBERG, *MULTINATIONAL CHALLENGE*, *supra* note 12, at 178.

81. *S.A. Société Fruehauf-France v. Massardy*, [1968] D.S. Jur. 147, 5 I.L.M. 476 (1966).

82. *Foreign Assets Control Regulations*, 31 C.F.R. § 500.329 (1985). The Russian gas pipeline affair involved an attempt by the Reagan administration to block construction of a natural gas pipeline from the Soviet Union to Western Europe. See Kenneth A. Rodman, *Sanctions at Bay? Hegemonic Decline, Multinational Corporations, and U.S. Economic Sanctions Since the Pipeline Case*, 49 INT'L ORG. 105 (1995).

territoriality principle applied.⁸³ Under the nationality principle, the Dutch subsidiary was a Dutch national. Under the protective principle, the “foreign policy interest” involved did not jeopardize the security or creditworthiness of the United States. Finally, the measure did not involve “direct and illicit effects within the United States.”⁸⁴

Since the pipeline debacle, the United States has generally not attempted to apply its trading with the enemy legislation extraterritorially, preferring other means of persuasion.⁸⁵ Thus, in terms of the matrix, this area falls into the right-side column on the horizontal axis, suggesting that the law must be applied extraterritorially to achieve its effect, but in the bottom row on the vertical axis, suggesting that countries and MNEs disagree. Extraterritorial application should thus be avoided unless agreement with major allies can be achieved first.

B. *Antitrust*

Antitrust is another area in which the United States was a pioneer in extraterritoriality. Initially, the Supreme Court held that the Sherman Act does not apply to conduct overseas.⁸⁶ In 1942, however, Learned Hand decided in *United States v. Aluminum Company of America* that a cartel concluded in Canada could be subject to U.S. antitrust law if it had “effects” in the United States.⁸⁷ The result has been a growing tendency to apply antitrust law extraterritorially, which has given significant offense to our trading partners.⁸⁸ The European Union also has applied antitrust law on an extraterritorial basis.⁸⁹

83. These exceptions are defined in the Restatement (Third) of Foreign Relations Law as the nationality principle, the effects doctrine and the protective principle. RESTATEMENT (THIRD) OF THE FOREIGN RELATIONS LAW (1987).

84. *Compagnie Européenne des Pétroles S.A. v. Sensor Nederland B.V.* (Dist. Ct. The Hague Sept. 17, 1982), 22 I.L.M. 66 (1983).

85. See Rodman, *supra* note 82, at 106 (arguing that in the cases of Nicaragua, Libya and South Africa, sanctions have been successful despite their lack of extraterritorial application). A notorious exception is the Helms-Burton Act, which does apply extraterritorially, but has been repeatedly suspended by Presidents fearing the foreign policy complications. Helms-Burton Act, Pub. L. No. 104-114, 110 Stat. 785 (Mar. 12, 1996).

86. *Am. Banana Co. v. United Fruit Co.*, 213 U.S. 347 (1909).

87. *United States v. Aluminum Co. of Am.*, 148 F.2d 916 (1945); for more recent cases, see, e.g., *Timberlane Lumber Co. v. Bank of Am.*, N.T., 549 F.2d 597 (1976); *Hartford Fire Ins. Co. v. California*, 509 U.S. 764 (1993).

88. See, e.g., Protection of Trading Interests Act 1980, 21 I.L.M. 834 (1982) (Eng.).

89. See, e.g., Case T-36/91, *Imperial Chem. Indus. (ICI) v. Comm'n*, 1995 E.C.R. II-

In the academic literature, there is general agreement that antitrust law must be applied on an enterprise-wide basis to be effective.⁹⁰ On the other hand, there is also general recognition that the interests and policies of countries diverge on antitrust issues. Some of this divergence is purely self-interested, as when the European Union almost blocked the Boeing-McDonnell Douglas merger to protect Airbus or when Japan and the United States both sided with their respective MNE in the Kodak-Fuji dispute.⁹¹ Other sources of divergence, however, are more principled. EU competition law tends to be more focused on protecting smaller market competitors than U.S. competition law, which focuses exclusively on efficiency and consumer welfare.

Thus, although there has been some measure of agreement on international cooperation regarding antitrust matters, this area still tends to fall into the bottom row on the vertical axis.⁹² Commentators tend to agree that work needs to be done to resolve such disputes because of the global reach of the issue.⁹³ They disagree, however, on the important question: What is the appropriate forum to resolve such disagreements?⁹⁴

C. Discrimination

In the area of gender discrimination,⁹⁵ a couple of U.S. Supreme Court decisions can illustrate the problem. In *Sumitomo Shoji America v. Avagliano*, the Court held that the entity approach applied to a discrimination suit filed by female employees of a wholly-owned U.S. subsidiary of a Japanese MNE. The key issue

1847; Case 89/85, *Ahlstrom v. Comm'n*, 1988 E.C.R. 5193; Case T-102/96, *Gencor Ltd. v. Comm'n*, 1999 E.C.R. II-753.

90. See, e.g., Eleanor M. Fox, *Antitrust and Regulatory Federalism: Races Up, Down, and Sideways*, 75 N.Y.U. L. REV. 1781 (2000); Daniel K. Tarullo, *Norms and Institutions in Global Competition Policy*, 94 AM. J. INT'L L. 478 (2000); Andrew T. Guzman, *Antitrust and International Regulatory Federalism*, 76 N.Y.U. L. REV. 1142 (2001).

91. Fox, *supra* note 90, at 1803-04.

92. See, e.g., EU-U.S. and other bilateral agreements, and the work of the WTO and OECD working groups. The U.S. guidelines for international antitrust recognize the likelihood of disagreement, as do the balancing tests applied by courts. See, e.g., *Timberlane*, 549 F.2d at 597.

93. See Fox, *supra* note 90, at 1802-06.

94. *Id.* at 1802-04 (advocating an independent competition forum).

95. For a general discussion of international women's rights theory, see Karen Engle, *International Human Rights and Feminism: When Discourses Meet*, 13 MICH. J. INT'L L. 517 (1992).

was whether the U.S.-Japan Friendship, Commerce and Navigation Treaty, a precursor to current Bilateral Investment Treaties (“BITs”) protected the employment practices of the subsidiary. The Court held that it did not provide such protection because the subsidiary was not a “company of Japan.” It is not clear how the Court would have analyzed the issue had the MNE operated through a branch.⁹⁶

Nine years later the Court faced a similar issue, but this time the situation was reversed. In *EEOC v. Aramco*, the issue was whether U.S. discrimination law applied to the actions of a U.S.-based MNE operating through a branch in Saudi Arabia and allegedly discriminating against a U.S. citizen employee. The Court held that it did not apply, and established a general presumption against extraterritorial application of U.S. law, unless Congress explicitly stated otherwise.⁹⁷

Aramco has been roundly criticized on several grounds. The finding that Congress did not intend Title VII to apply extraterritorially ran contrary to several strong indicators in the statute, and, in fact, Congress immediately overturned that aspect of the decision.⁹⁸ More importantly, commentators such as Larry Kramer pointed out that in *Aramco*, there was no real conflict with the policy of the host country, since it was unlikely that Saudi Arabia would object to a law forbidding religious and ethnic discrimination against people like the plaintiff—i.e., Muslims of Arabic descent.⁹⁹

However, one needs to take a broader view of the issue. Gender discrimination is an extremely loaded cultural issue, as is evidenced by the reservations of many countries to the International Convention on the Elimination of all forms of Discrimination against Women (“CEDAW”).¹⁰⁰ One can only imagine the response if the United States were asked not to apply its law on discrimination to Sumitomo Shoji on the grounds that Japanese norms on discrimination should apply extraterritorially, or suppose that in

96. *Sumitomo Shoji Am. v. Avagliano*, 457 U.S. 176 (1982).

97. *EEOC v. Aramco*, 499 U.S. 244 (1991). The scope of the presumption may have been narrowed by *Hartford Fire Ins. Co. v. California*, 509 U.S. 764 (1993). Ironically, in the same Term Chief Justice Rehnquist (who wrote for the majority in *Aramco*) also decided that the U.S. Drug Enforcement Agency could enter the territory of a sovereign nation and kidnap one of its citizens to bring him to justice in the United States—a far greater affront to sovereignty than was involved in *Aramco*. *United States v. Alvarez-Machain*, 504 U.S. 655 (1992).

98. See Civil Rights Act of 1991, Pub. L. No. 102-166, § 105, 105 Stat. 1071, 1074–75 (1991) (codified as amended at 42 U.S.C. § 2000e-2(k) (1994)).

99. Kramer, *supra* note 22, at 217.

100. See, e.g., Smolin, *supra* note 70, at 400–04.

Aramco, the issue was discrimination by Aramco against women in Saudi Arabia by not promoting them to jobs that require driving.

Thus, this Article argues that although discrimination law, like child labor law, falls in the middle column on the horizontal axis because one would like to see the law applied extraterritorially to all MNEs, caution is warranted. That is because, unlike in the child labor case, there is a real clash with deep-seated cultural norms of the host country. While in some cases, such as the Civil Rights Act of 1991, Congress may decide that the goal of the legislation is important enough and the likelihood of conflict low enough to warrant extraterritorial application, careful consideration needs to be given in each instance to the potential clash with host country interests in this area.¹⁰¹

VI. CONCLUSION: TOWARD A WORLD INVESTMENT ORGANIZATION

The results of the proposed matrix for the examples discussed above are as follows:

Y Axis				
	Countries and MNEs agree	Contracts	Corruption	Bankruptcy
	Countries agree but MNEs do not	Torts	Child Labor	Tax
	Countries disagree	Property	Discrimination	Antitrust & Trading with the Enemy
		Law does not require extraterritoriality	Law partially requires extraterritoriality	Law requires extraterritoriality X Axis

101. It helps, however, that the MNEs themselves are unlikely to want to engage in gender discrimination, since it narrows the pool of available human capital. The Civil Rights Act of 1991 provides for a “foreign compulsion defense,” for cases in which the statute would require the employer to violate the law of the foreign country. Civil Rights Act of 1991 § 109(b). But this defense may be too narrow. *See, e.g., Abrams v. Baylor Coll. of Med.*, 805 F.2d 528 (5th Cir. 1986) (holding insufficient the reasonable understanding of the host government policy); *Mannington Mills v. Congolenum Corp.*, 595 F.2d 1287 (3d Cir. 1984) (finding that mere approval or encouragement of conduct fails the actual compulsion test).

Comity, the case-by-case application of the enterprise approach, is the preferred outcome in the first column. Unilateral extraterritoriality with reciprocity is the preferred outcome in the top and middle rows of the second and third columns. Harmonization is the preferred outcome in the bottom row of the second and third columns.

Much of the debate on how to achieve harmonization has focused on the choice of an appropriate forum.¹⁰² In general, four candidates present themselves: the OECD, the United Nations Conference on Trade and Development ("UNCTAD"), the WTO, and a new WIO.

The OECD is the preferred forum for coordinating action when extraterritoriality with reciprocity is the preferred approach. In these cases (those in the top two rows), there is no real clash of interests among countries. Rather, the disputed issues resolve to questions of competitiveness, involving the reluctance to take unilateral action for fear of injuring domestic MNEs, and questions of sovereignty, involving the reluctance to cede to extraterritorial application even when there is no policy disagreement. As the corruption and tax examples above illustrate, the OECD is the best forum to resolve these issues because the overwhelming majority of MNEs are from OECD home countries. Thus, if the OECD acts as a whole, competitiveness concerns are abated. As for sovereignty, since investment flows among OECD countries are bilateral, reciprocity can be used to allay sovereignty concerns.¹⁰³

For truly disputed issues, the OECD is not the right forum because it excludes the developing world. This assertion has been well illustrated by the debate over the MAI. Ultimately, the MAI failed because of its exclusive focus on investor rights and neglect of investor responsibilities.¹⁰⁴ The OECD, which remains a "rich countries' club," is an inappropriate forum to negotiate agreements when there is a fundamental policy disagreement with developing

102. Examples include the debates in antitrust between Fox and Guzman, and in tax between Green and Slemrod/Avi-Yonah.

103. There may still be a sovereignty issue where the extraterritorial reach impacts non-member countries, but in my view this is not a serious concern if there is no underlying policy disagreement. Presumably, some transfer payment can be negotiated, as in the case of tax havens.

104. On the demise of the MAI, see, e.g., Peter T. Muchlinski, *The Rise and Fall of the Multilateral Agreement on Investment: Where Now?*, 34 INT'L LAW. 1033 (2000); Yoshi Kodama, *Dispute Settlement under the Draft Multilateral Agreement on Investment*, J. INT'L ARB., Sept. 1999, at 45, 46-52; Pippa Read, *International Investment in the WTO: Prospects and Challenges in the Shadow of the MAI*, 11 BOND L. REV. 360, 368 (1999).

countries.¹⁰⁵

For the same reason, UNCTAD must be rejected.¹⁰⁶ Its membership is as wide as the U.N., but it is too focused on the interests of the developing countries, as the failed attempt to negotiate a Code of Conduct for Transnational Corporations in the 1970s and 1980s indicates.¹⁰⁷ UNCTAD heavily focuses on investor responsibilities at the expense of investor rights.¹⁰⁸

The WTO presents a tempting arena. It has broad membership, with a significant voice for both developed and developing countries. It also has a broad agenda, which makes trade-offs possible even on highly contentious issues.¹⁰⁹ There are, however, serious problems with this organization. First, the primary mission of the WTO is focused on trade. While the line between investment and trade issues has blurred recently due to the focus on services through General Agreements on Trade in Services ("GATS")¹¹⁰ and FDI through Trade-Related Investment Measures ("TRIMs"),¹¹¹ the overlap is not complete.¹¹² Thus, commentators have pointed out that some tax and antitrust issues are more linked to trade than others.¹¹³ There is a danger of overwhelming the WTO with issues unrelated to its core mission and expertise, although that mission, and the WTO staff, could perhaps be expanded to address this problem.

More importantly, the WTO has a well-developed judicial dispute resolution mechanism. While this characteristic is one of its main advantages, there is a danger in extending such a mechanism to

105. The OECD has thirty members. With the exceptions of Mexico and South Korea, none are developing countries. For a list of the membership, see the OECD website at <http://www.oecd.org>.

106. On UNCTAD, see WORLD INVESTMENT REPORT 2002, *supra* note 2, at ii.

107. Muchlinski, *supra* note 104, at 1037.

108. *Id.*

109. Andrew T. Guzman, *Is International Antitrust Possible?*, 73 N.Y.U. L. REV. 1501, 1545-46 (1998).

110. General Agreement on Trade in Services, Final Act Embodying the Results of the Uruguay Round of the Multilateral Trade Negotiations, Apr. 15, 1994, [hereinafter Final Act] LEGAL INSTRUMENTS—RESULTS OF THE URUGUAY ROUND vol. 1 (1994), 33 I.L.M. 1125, 1168 (1994) [hereinafter GATS].

111. Agreement on Trade-Related Investment Measures, Final Act, *supra* note 110, Annex 1A, 33 I.L.M. at 1153 [hereinafter TRIMS].

112. These two agreements, GATS and TRIMS, are the product of the Uruguay Round that established the WTO on January 1, 1995. See Agreement Establishing the World Trade Organization, Final Act, *supra* note 110, 33 I.L.M. at 1144.

113. See Joel Slemrod & Reuven Avi-Yonah, *(How) Should Trade Agreements Deal with Income Tax Issues?*, 55 TAX L. REV. 533, 547-48 (2002); Fox, *supra* note 90, at 1788.

areas in which disagreement is more basic than in the trade context. The risk is that countries will ignore the decisions of the WTO Appellate Body and the whole enterprise will unravel. In fact, the strong dispute resolution mechanism in the draft MAI was one of the main reasons for its failure.¹¹⁴

What is needed is a forum that has broad membership with strong representation from both developed and developing countries; a broad agenda making "horse trading" possible; and representation for MNEs, who can bring pressure to bear when they perceive harmonization to be in their interests, and NGOs, who can bring pressure when MNEs disagree. In addition, the forum should operate under a consensus rule similar to the pre-1994 GATT.¹¹⁵ That is, if a member feels that its sovereignty is too adversely affected by a dispute resolution determination, it can block it, but at a reputational cost that in practice ensures that such blockages will not occur too frequently.

Such a body has been proposed in divergent areas such as antitrust¹¹⁶ and tax.¹¹⁷ One goal of this Article has been to show that these areas present some similarities and therefore a single organization, the WIO, may be appropriate to cover both, as well as other areas in which harmonization is the preferred outcome. Harmonization may, in fact, be difficult to achieve, but partial progress may be possible even in the difficult areas.

Legislators and courts frequently need to decide if national laws should apply to MNEs as a whole or only within their territory. This Article has suggested a way to analyze the relevant issues and to help focus time-consuming efforts to harmonize national laws on those subject areas where harmonization is truly necessary.¹¹⁸ In other areas, extraterritoriality is either not needed or can be applied unilaterally. Hopefully, the analysis presented above can be a useful framework for addressing the difficult question of how national laws should apply to enterprises operating beyond national borders.

114. Kodama, *supra* note 104, at 46–52.

115. General Agreement on Tariffs and Trade, Oct. 30, 1947, 61 Stat. A-11, T.I.A.S. No. 1700, 55 U.N.T.S. 186.

116. Fox, *supra* note 90.

117. Vito Tanzi, *Does the World Need a World Tax Organization?*, in *THE ECONOMICS OF GLOBALIZATION* 173 (Assaf Razin & Efraim Sadka eds., 1999).

118. One of the reasons the MAI failed is that its reach was too broad. A MAI that is more focused may have a better chance of success. See Muchlinski, *supra* note 104, at 1037–46.