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Principles for Policymakers

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Multinational corporations are global goliaths, but they have not conquered the world, nor are they responsible for every economic ill, as is sometimes alleged. These firms contribute to global prosperity by improving productivity and efficiency, innovating, and creating jobs—mostly good jobs—in both home and host countries. Governments lavish attention on multinational corporations, seeking the good that accompanies their investments even as policymakers worry about the influence multinational firms have on the local environment, social conditions, and politics. In this regard, governments face the tradeoffs that commonly afflict economic policymaking. Efforts to control the actions of multinational firms typically come at the cost of reduced investment, thereby reducing the contributions of these firms to local economies. This tradeoff is particularly stark when, as is often the case, governments compete with each other to attract multinational firms.

Multinational corporations also have substantial market and political power that they can, and often do, use to reduce their tax bills, thwart competitors, and influence regulation, legislation, and trade agreements to their particular advantage. To promote the general welfare, governments should and do monitor their activities and, when appropriate, regulate them by national rules and laws and by international agreements. Drawing from the available evidence in this volume and elsewhere, this chapter offers several principles for public policy toward multinational corporations. Our objective is to encourage policymakers to protect and, indeed, encourage those activities of multinational corporations that contribute to rising living standards around the world while restraining activities that thwart competition or exacerbate social ills and inequities. This chapter represents the views only of its three authors, not other contributors to this volume—although it does draw on their work.

PRINCIPLE 1: Governments should avoid erecting barriers to realizing benefits that multinational corporations offer modern economies. They should avoid tariffs, punitive regulations, and taxes directed at foreigners, and other restrictions on the movement of goods, people, investment, and data across borders.

Multinational corporations contribute to investment, innovation, employment, productivity, and other dimensions of economic performance by integrating their operations throughout the world. The economic benefits created by these firms accrue to countries rich and poor, notwithstanding certain multinational practices in low-income countries and the economic harm suffered by some workers and communities in high-income countries.

The prosperity of high-income economies relies on multinational firms, whose international operations enhance capital and labor productivity. Much multinational production still occurs in high-income countries, belying the caricature of the modern multinational as choosing only the lowest-cost production locations. As colorfully described by Davies and Markusen in chapter 2 in this volume, typical multinational production is less like a snake that moves production along a value chain from one low-cost location to another and more like an octopus, reaching out to perform similar activities in multiple locations across the globe, often to serve local markets. Evidence offered in chapter 6 in this volume by Oldenski shows that when a U.S. multinational expands its employment abroad, it typically, though not always, expands employment in the United States. Consequently, efforts by governments to prevent their resident multinational firms from investing abroad are unlikely to improve economic conditions either at home or abroad.

Multinational corporations depend on the free movement of goods, services, ideas, people, and data. International operations function most smoothly when firms can draw on resources available elsewhere. The multinational business model, which relies on deploying firm-specific capital and internal transactions to create value in multiple locations simultaneously, is impossible to implement properly without fluid movement. Governments that create barriers at their borders throw sand in the gears of this otherwise highly functioning economic machine, and in the process do their economies significant harm. Governments often are tempted to limit the penetration of foreign multinational firms in their economies, in efforts to preserve the competitive positions of domestic companies to maintain their employment and as bulwarks against monopoly; in fact, openness to foreign direct investment may be the best way to create good jobs, spread innovation, and spur market competition.

Claims that national security concerns justify imposing limits on multinational investment and restrictions on research activities of multinational firms, including whom they employ, require careful and skeptical scrutiny. Multinationals creating particularly advanced technologies in certain strategic sectors, such as communications and defense, could face situations in which their commercial interests conflict with national security interests, and these situations create needs for policies and processes that would then limit the actions of multinational firms. But these are unusual situations, whereas there are apt to be many such claims by those seeking to limit market competition in order to benefit from protection.

For all of the employment, investment, R&D, and other economic contributions that multinationals make, many countries have not fully realized the potential economic benefits of multinational operations. Lower-income countries, in particular, do not currently attract the investment and employment levels of higher-income economies. Yet it is in less affluent economies that multinational firms have the greatest ability to contribute to economic welfare, since the employment opportunities, economic openness, and exposure to the rest of the world that they foster can be extremely valuable if properly managed.

PRINCIPLE 2: Governments and multinational corporations should adopt policies and practices that ensure that all segments of society benefit from the activities of multinational corporations and from globalization more generally.

While the net effects of the activities of multinational corporations, and globalization more generally, are positive, there are costs. These costs are disproportionately borne, at least in developed countries, by less educated workers, particularly those who perform routine tasks that are easily moved offshore or automated. Within countries, this has contributed to a worrisome increase in inequality in recent decades. At the same time, labor's share of income—both in the United States and globally—has declined, and many measures of median income and wages have stagnated. Globalization and the activities of multinational corporations are not the only factors driving these trends, but they have played a role. For all the discussion of "compensating the losers," efforts that have been made in the United States through Trade Adjustment Assistance and worker training programs have been inadequate. The regional economic dislocation associated with abrupt plant closures or imports of low-cost foreign goods can be severe, even if more than offset by gains elsewhere in the economy.

The solutions involve spending more money and spending it more wisely and creatively, and in experimenting with such programs as wage insurance, flexible training subsidies, and other measures targeted at individuals and communities who have not enjoyed the benefits of globalization. Multinational corporations and their executives should support—and be willing to pay taxes to help finance—such public efforts. Moreover, multinational corporations need to invest more in training to better equip their employees to cope with a rapidly changing economy.

The pain borne by individuals, families, and entire communities is reason enough to pursue different policies, but it also threatens the post–World War II political consensus that produced decades of peace and rising living standards around the world. Governments that stand idle in the face of such severe economic pain risk popular backlash. Multinational corporations that do not assume responsibility for their actions—that do not identify and remedy the unwelcome side effects of their actions—not only betray the standards they publicly proclaim for themselves and risk vilification, but also undermine support for economic policies from which they benefit, fuel the rise of populist politicians, and put their future prosperity at risk. As the Business Roundtable noted in updating its "statement on the purpose of a corporation," the stakeholders of a corporation are not only their shareholders, but also their customers, employees, suppliers, and communities.[1]

Public opinion plays an important role in determining economic policies in democratic societies. Over time, public attitudes about multinational corporations have soured. In the United States, the Gallup Organization's annual survey finds that in the 1970s, an average of 31 percent of respondents reported having either a "great deal" or "quite a lot" of confidence in big business. By the 2010s, the fraction reporting these favorable opinions had fallen to an average of 21 percent. In this environment, it can be challenging for democratic governments to strike arrangements conducive to extensive multinational investment, notwithstanding the economic benefits such investment may bring. Multinational corporations that ignore this deterioration of public trust put themselves at risk of policies that will not only hurt their profits but restrain their capacity to innovate and improve global productivity.

In developing countries, as Aisbett and others note in chapter 7 in this volume, there is evidence that multinational corporations violate workers' rights, including discriminating by gender and preventing workers from organizing unions. This suggests that managements of multinational corporations everywhere need to address the conditions of those they employ around the world and those who work for companies on whose labor they depend, and that governments need to consider working conditions when they strike global trade agreements.

PRINCIPLE 3: Governments should cooperate to formulate consistent, cohesive policy frameworks because what happens in one place influences what happens elsewhere. These policy frameworks should respect the right of sovereign nations to reflect the preferences and needs of their people.

To this end, policymakers should strengthen multilateral institutions that regulate international trade and investment, fixing their shortcomings and adapting them to the evolving global economy. Trade and investment disputes should be resolved more quickly. Trade rules should be extended to cover a broader set of services, and policies should be written to account for the growth of e-commerce. Guidelines on the appropriate role of government in promoting and supporting businesses should be negotiated. International investment and trade regulations that serve favored corporate interests but do not promote general economic welfare should be removed.

Because they span country borders, multinational firms can transmit economic shocks from one part of the world to others. National regulators must, therefore, remain aware of their country's exposure to policy actions and economic conditions elsewhere. For example, lax financial regulation in one country can increase the fragility of the banking systems of others. Policymakers should incorporate insights related to these transmission mechanisms and coordinate efforts to make global systems more robust.

There is also a need for greater coordination of antitrust policy. Many large firms that face accusations of engaging in anticompetitive practices are multinational firms. But antitrust authorities in different jurisdictions have divergent regulations and objectives. This diversity is further complicated when governments choose to support and subsidize national champions in some industries. Authorities should cooperate when collecting and analyzing evidence of anticompetitive behavior. Basic questions regarding how to define the boundaries of a relevant market are complicated in an international context, because even just the threat of foreign competition can affect behavior. Antitrust issues are particularly nettlesome in parts of the technology sector that are subject to large economies of scale and network externalities that make a network more valuable if more people are connected to it. Furthermore, many offerings in this sector can be accessed from anywhere. These features require a coordinated approach to determine what regulations should be applied and what constitutes evidence of inappropriate behavior.

Climate change presents an enormous challenge. No matter how much one company or one country does to reduce emissions, it cannot effectively reduce the dangers of climate change unless other companies and other countries join in the effort. Public policy can and should find ways to make private actors shoulder the cost of their contributions to greenhouse gas emissions; the obvious options include carbon taxes and cap-and-trade permit systems. Multinational corporations, many of which have announced climate-related goals, can and should support and help design such government efforts. National governments—and multilateral organizations—should use their leverage to get other governments to cooperate in what must be a global effort.

PRINCIPLE 4: Innovation is an important contributor to prosperity, so governments should pursue policies that encourage multinational corporations to pursue innovations and share the benefits with the world.

Innovation is a critical driver of economic growth and the accompanying rising living standards around the world. The process of innovation has become more global over recent decades. Multinational corporations are major innovators, and their efforts are the products of contributions by the best minds from every part of the world, rich and poor countries alike. As chapter 8 in this volume, by Branstetter, Glennon, and Jensen, illustrates, the rise of economic nationalism, the aggressive use of tariffs, the opposition to immigration, and new restrictions on cross-border flows of data all threaten to limit rates of innovation and adoption of new goods and ideas. Therefore, policies that enable the general operations of multinationals—policies that support the free flow of goods, services, human capital, and data—also are essential to supporting innovative activity. Innovations are often embodied in goods like new scientific equipment, and trade in these goods allows innovations to spread, facilitating further innovation. Immigration of highly educated foreign nationals, many of whom came to the United States for college or graduate school, plays a significant role in innovation that occurs within the United States; other countries have similar experiences. This role of immigration calls for legislation making it easier for foreign students to obtain work visas upon graduation. Policies that make it harder for foreign individuals to stay in the United States would impede research and, in turn, induce U.S. multinationals to locate more of their innovative activity abroad.

Strong and strictly enforced intellectual property rights are essential to provide incentives for multinationals to invest in innovation. Such rights also give multinationals comfort in transferring technology to their foreign affiliates and in shifting research and development efforts abroad. While governments should commit to defending intellectual property rights, there are limits to how far these rights should extend. Corporations can abuse the patent system, protecting monopoly profits far beyond the period of exclusivity required to provide incentives for innovation. Governments should limit the ability of patent trolls to obtain intellectual property rights in a manner that limits innovation. And policy should ensure that innovations such as life-saving drugs are widely accessible even in markets where income levels might limit their availability.

PRINCIPLE 5: Governments should forge consensus on principles governing the taxation of multinational corporations.

Governments struggle in their efforts to craft appropriate taxes on multinational corporations amid widespread concern that multinational corporations pay very little in taxes, manipulate their accounting to exploit tax havens, and thereby starve governments of badly needed revenue. As chapter 10, by Dyreng and Hanlon, and chapter 11, by Dharmapala, in this volume indicate, firms do structure their affairs in ways that reduce their tax liabilities, but the more spectacular claims of lost tax revenue have flimsy empirical support and are inconsistent with the reality that multinational firms collectively pay considerable taxes. Both chapters note that self-help is not the only source of multinational tax reduction. Over time, governments have reduced their tax rates and enacted other tax provisions designed to make their countries attractive locations for multinational firms, including by a reluctance to adopt measures that would diminish the impact of tax-haven operations.

Governments need tax revenue and feel pressure from reform advocates and domestic business and labor lobbies, all of which argue for heavier taxation of multinationals; but they are also lobbied by multinational corporations and are loath to risk losing the employment, productivity, and other benefits that multinationals bring. Furthermore, there is conflict between governments, which frequently disagree over which country has the right to tax profits made by firms whose operations lie in many countries—and whether certain types of taxes are legitimate under international agreements. The governments of multinational home countries often bristle at taxes imposed by countries where their multinationals have operations, the most recent prominent example being the U.S. reaction to digital taxes imposed by several other countries that are alarmed by the rising presence of U.S. digital firms described by Edelman in chapter 9 in this volume.

All countries stand to benefit from establishing agreement over principles that govern the taxation of multinational corporations. These principles should identify the types of taxes covered and identify in which countries, and under what circumstances, governments have rights to tax income. This does not entail agreement over tax rates but instead over taxing authority—and, in particular, the extent to which income is appropriately subject to taxation by the countries in which multinationals are based and the countries in which they have foreign operations. In the present environment, it is often unclear whether and to what extent firms earn income, and when they do, where the income was earned and to what extent it may have been taxed. Too frequently, countries feel that they are missing out on tax revenue that is legitimately theirs, which puts them in conflict with taxpayers and other governments, and drives them to consider expedients that do not represent sound policy. With agreed-upon principles, each country can better understand the scope of its legitimate taxing authority, cooperate with other governments in enforcing its taxes, and make reasoned choices over appropriate levels of taxation, given all the tradeoffs that taxing business income inevitably entails.

PRINCIPLE 6: Governments should invest in collecting more and better data about the activities of multinational corporations.

The availability of reliable and robust data is a necessary, albeit not sufficient, condition for good policy and for informing a public debate that is too often influenced by anecdotes. This volume relies heavily on data compiled by the U.S. Commerce Department's Bureau of Economic Analysis. These data are unique in their coverage of the financial and operating activities of multinational parent firms as well as each of their foreign affiliates. They cover U.S.-based multinationals and foreign-based multinationals with interests in the United States. Very few countries dedicate resources to conducting surveys of multinationals operating within their borders, making it hard to understand these firms, never mind regulate them. U.S. data collection efforts face threats of budget cuts that would raise reporting thresholds and reduce the extensiveness of reporting. It is imperative that statistical agencies receive the resources they need to measure the activities of multinationals; policy makers, business managers, and the general public depend on it.

In response to the OECD Base Erosion and Profit Shifting Project, many countries are introducing legislation that requires firms to provide tax authorities with country-by-country reports of financial tax data. These data have the potential to increase transparency regarding basic measures of economic activity as well as tax payments in different jurisdictions. Governments should create opportunities for researchers to access and analyze the data that are collected as a part of this and other efforts.

Private sector organizations have emerged as providers of data on multinationals. The Orbis dataset compiled by Bureau van Dijk provides some income statement and balance sheet information covering the operations of parents and affiliates based in more than 30 developed and developing countries. The WorldBase data compiled by Dun & Bradstreet cover establishments in more than 205 countries and territories, providing basic information about the industries of multinational affiliates and the scales of their activities. Private data can supplement and improve the accuracy of government-collected data, but they cannot substitute for the breadth, historical continuity, and integrity of publicly gathered and distributed data.

Additional effort should also be dedicated to tracking more extensively forms of multinational activity that have likely grown in recent decades and present distinctive policy considerations. For example, anecdotal evidence suggests that a considerable fraction of international activity occurs on a long-term contractual basis that is distinct from an ownership relationship or a spot market transaction. Under these relationships, a multinational parent might contract for manufacturing to occur in one location at an establishment it does not own, while distribution occurs in a separate set of owned wholesale or retail locations. More and better data on such global supply chains that stretch between unrelated firms would improve our understanding of these production processes and inform relevant public policies.

CONCLUSION

The benefits and risks of the activities of multinational corporations call for thoughtful and rigorous regulation. Multinationals can have enormous impacts on real income levels, the products and services that people consume, and on quality of life. However, the size and scale of these firms position them to take advantage of aspects of the global economic system in a manner that promotes narrow corporate self-interests. Well-designed policies are required to allow the free movement of economic factors so that multinationals can operate efficiently while at the same time protecting those who lose out when efficiency gains are realized. The cross-border nature of multinational firm activity necessitates that policies be coordinated across jurisdictions, particularly policies related to innovation and taxes. And the formulation of well-designed policies depends on our understanding the activities of these firms, an understanding that can only be obtained with extensive financial and operating data that characterize their behaviors. Given the extent of public skepticism about multinationals despite the benefits they create, it is imperative that regulators take further action to address the risks posed by multinationals now.

NOTES

1. Business Roundtable, *Statement on the Purpose of the Corporation*, August 19, 2019, https://opportunity.businessroundtable.org/ourcommitment/.