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Current Proposals for Marshalling Data on and Disclosure by Multinationals

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It is a truism that the development of effective legislation—national or international—regulating conduct of persons subject to national jurisdiction is impossible until the legislator has a full grasp of the nature of the conduct in question and its social effects. Current efforts to construct an international code of conduct for multinational enterprises exemplify the point: there is hardly a consensus—much less data—on the nature of the transnational phenomenon or its habits although there is considerable rhetoric. Accordingly, the United Nations Commission on Transnational Corporations in the Report on its Second Session, March 1-12, 1976,[1] listed as the second area for the focus of the program of work, after formulation of a code of conduct, "establishment of a comprehensive information system."[2]

The Commission then issued a directive to its technical organ, the Information and Research Centre on Transnational Corporations, as to its target in the establishment of such an information system. This directive is most interesting in that it acknowledges not only the absence of data, but the constraints on the data gathering process, and even the paucity of information concerning those constraints. The constraints can be classed into two major types: positive and intellectual. As stated in the Commission's Report, the positive constraints are, "existing national legislation and regulations" and the "requirements of business confidentiality."[3] What the Commission meant, of course, by "existing

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[1]Comm'n on Transnational Corporations, U.N., Report on the Second Session, March 1-12, 1976, reprinted in 15 I.L.M. 779 (July 1976), cited hereafter as Report of the Second Session.

[2]*Id.* at 781.

[3]*Id.* at 783.

national legislation" is not so much legislation forbidding disclosure by corporations subject to its jurisdiction, as the lack of national legislation requiring disclosure to an appropriate authority of information concerning activities of the transnational corporation which might be the appropriate subject matter of an international code of conduct. (The Commission recognizes that even if disclosure is required to a national authority, the passing on of such information to an international research center collecting data as a basis for possible international regulation runs counter to a state's economic interest in the competitive advantage to its entities of secretiveness; hence the reference to the "requirements of business confidentiality.") The Centre, therefore, is directed by the Commission to undertake a "feasibility study" on the subject of the availability of information to determine, among other issues, "the various disclosure problems and restrictions existing both at the private and governmental levels, including business confidentiality" and "the scope and nature of information which is now publicly available and that which may not be available because of its confidential nature."[4] In this connection, the Commission suggests that the Economic and Social Council invite all states to cooperate with the Centre in its task of collecting information, and goes so far as to remark that

> For this purpose, home and host countries may find it useful to examine the adequacy of their domestic legislative and regulatory powers to obtain and make available to the Centre relevant information from transnational corporations about their operations and activities.[5]

With respect to the positive constraints on data gathering, the above admonition to states may be the furthest that the international community is able to go. The Commission was able to list, in Paragraph 23 of its report,[6] the subject matter areas where the need for information on behavior is most pressing, and the areas are those addressed in the present Symposium; but for the moment any proposal for international reporting requirements would seem to be premature. The reason for this may be the classic dilemma of international politics: an international forum will express as an international norm only the lowest common denominator. Since there presumably is at present no consensus among states on the degree of compulsory reporting that it is socially desirable for a home country to demand of its business corporations, the most that can be asked of the members of the Commission is that they review their legislation. Even this, for example, is further than the Organization for Economic Co-operation and Development in its consideration of the conduct of multinational enterprises subject to the jurisdiction of its member states has been willing to go.

[4] *Id.* at 784.
[5] *Id.* at 785.
[6] *Id.* at 784-785.

The Declaration on International Investment and Multinational Enterprises, released June 21, 1976[7] by the O.E.C.D., does not even mention positive legislation on disclosure (except to the extent that the call in Paragraph II.1 of the Declaration for "National Treatment"[8] means that no more disclosure should be demanded of a "Foreign-Controlled Enterprise" than is required of a domestic enterprise). The Guidelines for Multinational Enterprises that accompany the Declaration seem to the present writer to suggest that the political will for consensus on positive requirements of disclosure is absent in the O.E.C.D. nations. Rather than suggesting to the member countries that they work together or at least consult in the development of an information system, the Guidelines make clear that disclosure is considered a matter of information for investors, *not* for prospective regulators. Thus the Guidelines on Disclosure of Information list the suggested "financial statements and other pertinent information"[9] that enterprises "should, having due regard to their nature and relative size in the economic context of their operations and to requirements of business confidentiality and to cost, publish in a form suited to improve public understanding. . . ."[10]

This is not to suggest that a declaration by a group of countries as to the desirability of voluntary sunlight on financial operations by multinational enterprises is counterproductive; certainly the establishment of an international norm on the annual publication of financial statements is desirable. But it is also necessary to point out that the Guidelines' list of pertinent information that enterprises "should disclose" includes only one area of the entire list that the Report of the Commission on Transnational Corporations gave as the areas "where information gaps are most pressing": the Guidelines suggest the publication by multinational enterprises of "the policies followed in respect of intra-group pricing."[11] The Commission is interested in "transfer pricing, including its relation to taxation"; the Commission also lists as areas of information gaps: short-term capital movements by transnational corporations, restrictive business practices, political activities, and so on.[12] The Guidelines do urge from multinationals "a statement of the sources and uses of funds by the enterprise as a whole,"[13] while the Commission would like collection of information as to "relative use by transnational corporations of home country, international and host country financial markets in their operations and investments";[14] but the

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[7]Reprinted in 15 I.L.M. 967 et seq. (July 1976). The accompanying Guidelines for Multinational Enterprises are reprinted at p. 969 et seq. and will be cited hereafter as Guidelines.

[8]Declaration at 968.

[9]Guidelines at 973.

[10]*Id.* at 972.

[11]*Id.* at 973.

[12]Report of the Second Session at 784-785.

[13]Guidelines at 973.

[14]Report of the Second Session at 785.

difference in focus between the two groups of nations on the purpose and function of disclosure is clear. Even the list of constraints in the Guidelines' call for voluntary disclosure is larger than that of the Commission's; the quotation above refers not only to the requirements of business confidentiality but also to *cost* of disclosure and publication. The Guidelines' provisions on disclosure well illustrate, it is believed, the lack of political consensus on the extent to which disclosure *should* be required and in what areas; and that, at present, there is no international norm as to positive constraints or positive requirements.

Nonetheless, this note began by suggesting that constraints on the data gathering process consisted of two classes: the positive constraints discussed above and another class, intellectual constraints. This second class of constraints is recognized in the Report of the Commission and should be of considerable interest and concern to scholars and practitioners as well as rule-makers. Unlike what may be called the positive constraints, which ultimately require political and economic consensus—a rapprochement of ideology—for their resolution, the intellectual constraints can be developed by all those interested in a better functioning world community. The process of information gathering requires not only the authority to require information that is not voluntarily disclosed, but also a methodology. If twelve different jurisdictions require information in twelve different forms, no Centre can create a comprehensible aggregation of the information because an essential element is missing. To compare, for example, currency movements, it is necessary to have a numeraire: that numeraire can be the weight of gold or an S.D.R. or any number, but it must be agreed upon. So too with international information gathering concerning the activities of multinational enterprises: not only must good *useful* questions be asked, a form of replies must be agreed upon so that the results from one jurisdiction can be used with the results from another. At present, the intellectual constraints facing the Centre on Transnational Corporations in its assigned task of collection of information on the transnational enterprise are both the lack of good questions and the noncomparability of what information is available. This explains why the Commission's Report directed the Centre to undertake a feasibility study, "consulting the Expert Group on International Standards of Accounting and Reporting as the Centre may deem necessary" and to consider "the need for and feasibility of advancing towards a harmonization of national disclosure requirements."[15] The Expert Group is a technical group established in accordance with the report of the Commission on its first session, March 17-28, 1975,[16] which met in Geneva, August 30-

[15]Report of the Second Session at 784.
[16]Official Records of the Economic and Social Council, Fifty-ninth Session, Supplement No. 12 (E/5655).

September 10, 1976 and is expected to publish in the Spring of 1977 a report on not only international standards of accounting, but also a report which will concern itself with non-financial reporting.[17] This task, the establishment of international standards for the harmonization of the disclosure of information by transnational corporations, if well accomplished should result in the removal of a major constraint on the entire process of constructing an international code for the regulation of the transnational enterprise: the lack of adequate information on the phenomenon. For even if the political will is there to require disclosure, the results of disclosure will be only as good as the questions; and there is need for international consultation and cooperation on the way in which to ask questions, a need which one hopes the Expert Group is fulfilling.

In this connection, it had been hoped in the present note to report on a United States experiment in data gathering, particularly data gathering on the role of United States multinationals in short-term capital movements. In 1973, the Proxmire Amendment to the Par Value Modification Act[18] directed the Treasury Department to collect information from major United States multinationals on their foreign exchange dealings. Senator Proxmire was interested in collecting data to determine to what extent multinational dealings in the foreign exchange markets might be contributing to destabilization of the exchanges.[19] The Treasury has been collecting data under regulations which it published in final form in October, 1974. It is understood from conversations with Treasury officials that a compilation of data collected under the so-called "Foreign Currency Reports" is being made and presently is expected to be published in the *Treasury Bulletin.* At the time of the publication of the forms in their proposed form, the present author questioned the utility of information which would be gathered under them.

The United States has served as the leader in another area of multinational disclosure, and although no empirical study to back up the allegations has come to this writer's attention, it has been suggested that the new United States accounting rules with respect to *reporting* of foreign exchange gains and losses may be affecting the substantive behavior of the reporting firms with respect to their foreign exchange transactions. If this is so, it is an important consideration to be taken into account in the formulation of international reporting standards. In that formulation of disclosure standards, the formulators must ask not only "Is this a good useful question?" but "Is this a mode of reporting which will lead the enterprises into 'window dressing,' as attempts to dress up

[17]Conversation with W. T. Wang, Assistant Director in Charge, Information Analysis Division, Centre on Transnational Corporations.

[18]31 U.S.C.A. § 449 (1976). *See* Lichtenstein, *Treasury's New Reporting System for Information on Foreign Exchange Transactions,* 9 INT'L LAWYER 499, for the history of the amendment and an analysis of the proposed regulations under it.

[19]*See* Lichtenstein, *Loc. cit.*

one's public financial posture are called, and will this window dressing have economic effects on the international community?"

The United States action which leads to this inquiry was the promulgation in 1975 by the United States arbiter of accounting standards, the Financial Accounting Standards Board, of its Statement of Financial Accounting Standards No. 8—accounting for the translation of foreign currency transactions and foreign currency financial statements.[20] It is impractical in a paper of this size to explain the technicalities of the requirements of Statement No. 8, but its general effect can be briefly stated. Companies publishing in the United States financial statements denominated in dollars will report fewer dollars earned if certain net assets held in foreign currencies have depreciated in terms of the depreciation of that currency against the dollar; they will report gains in earnings if in translation in accordance with the statement the foreign assets have appreciated against the dollar. The point to note is that the gains and losses are *unrealized:* the foreign assets or liabilities are not being *converted* into dollars or even disposed of abroad; it is simply that their dollar value has changed between reporting periods because of a change in the relationship of the dollar and the foreign currency; and this change (occasioned by floating rates) is required by Statement No. 8 to be reflected in dollar reports of earnings. Well and good; evidently the Financial Accounting Standards Board felt that this method of reporting on foreign holdings would be more truly representative of the financial portrait of the entity. So long as everyone understands the standard—and it causes, as it is intended to, harmonization of the methods of accounting for foreign transactions—it should make for better public understanding of the financial condition of multinationals.[21]

There is, however, another problem. Managers of publicly owned companies are as concerned with the *reported* earnings of their companies as with the real economic position. The managers believe that it is the report and not the reality that affects the stock market price of the enterprise's stock and it is *that* fever chart by which they tend to judge the health of the enterprise.[22] Thus they will, possibly, be tempted to respond to Statement No. 8's requirements by managing the balance sheet of foreign affiliates so as to increase *translation* gains and avoid *translation* losses. Indeed the study by David Hale includes a section entitled "Balance Sheet Management" which instructs on just how, in

[20]Reprinted in the J. OF ACCOUNTANCY, December 1975 at 78; cited hereafter as Statement No. 8.

[21]For those who need an excellent explanation of the requirements, an investment banking firm, Bache, Halsey, Stuart has printed a Basic Study by David Hale: *Security Analyst's Guide to Foreign Currency Translation: The Impact of FASB 8 on Multinational Companies,* which explains in detail the changes that will be required in financial reporting by companies under Statement No. 8.

[22]See ROBBINS AND STOBAUGH, MONEY IN THE MULTINATIONAL ENTERPRISE (Basic Books, 1973), a study based upon interviews with managers in 187 multinational firms.

light of the reporting requirement, those results may be achieved. He notes that companies with highly leveraged foreign subsidiaries will benefit (on paper, of course) from devaluations and lose from revaluations. Ideally he notes that in addition to leveraging by borrowing in local currency, "the company must find some way to protect the resulting cash from devaluation." The best way, of course, is to export the local borrowing and invest it in a country with a strong currency. In his view, the problem "with any of these policies is the laws of the country in which a company is operating. Some countries, especially countries with weak currencies, do not permit export of capital. Some countries also discourage multinationals from relying too extensively on the local borrowing system for finance, preferring instead that the company bring new capital into the country."

That is the heart of the problem. If a country is a developing nation, or a nation with a weak currency, it seeks to encourage the inflow of capital, and to discourage the use of its financial resources for investment elsewhere. Mr. Hale seems to be suggesting that the balance sheet exigencies, that is, the substantive policies that managers will want to follow in order to produce better-looking financials when prepared in accordance with Statement No. 8, are policies which, from the point of view of the host countries concerned, are anti-developmental policies. This is suggesting that policies adopted for the appearance of reports are policies which may have detrimental economic effects on the international economic order. Certainly the protections which Mr. Hale suggests against translation gains and losses could, if in fact utilized by companies, contribute to the instability of the exchanges, that is, put downward pressure on a currency expected to go down and upward pressure on one expected to go up. We do not know, of course, that multinationals will in fact adopt substantive policies in order to avoid the new effects of Statement No. 8's translation rules in their United States financial statements. Whether they do so or not will be revealed in time by Treasury's Foreign Currency Reports if that reporting system *is* effective. But whether or not multinationals do adopt financial policies for reporting effects, the risk that they may do so, and the possible economic effects of such action, should be a consideration for any Group of Experts. There is no indication that the Financial Accounting Standards Board in its deliberations on Statement No. 8 took into account the possible effect of the requirements on host nations; hopefully an international Group of Experts will be more open to international ramifications of reporting standards.