Multinational Corporations and Governance of Political Activity

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Abstract:

This article builds a conceptual framework to help explain the political behavior of multinational corporations (MNCs). I build on three streams of literature, i.e. heterogenous firms, global value chains, and governance, and provide an overarching framework to help understand firms' political activities undertaken across value chain networks. I put forward a model that outlines MNCs' coordination of political mobilization using their affiliates and subsidiaries in different jurisdictions and demonstrate models of governance they have at their disposal to reach political goals. I argue that the spread of global value chains allows firms to develop legal links with enterprises across borders through which they orchestrate political activity or delegate policy goals. The degree of flexibility between MNCs and associated firms determine the model of governance they undertake with corporations in their network. They engage in such costly coordination either to obtain legal standing in foreign jurisdictions or to cultivate a sort of critical mass that goes after a policy objective. I demonstrate the plausibility of my propositions with anecdotal evidence and identify future lines of research.

Multinational corporations, governance, global value chains

Introduction

One of the key developments in global economic governance has been the spread of global value chains (GVCs) and the multinational corporations (MNCs) that operate across these complex networks. Indeed, more than half of exports and imports of goods between the largest economies was reported to take place within value chain networks and an estimated 80% of such GVCs center around MNCs (OECD, WTO, and UNCTAD 2013). MNCs sit at the center of the global economy and contribute to the lion's share of economic activity in the world. In 2014, they were responsible for over 50% of exports and imports in the world and accounted for one third of world's production output (OECD 2018). In the past, MNCs in the United States (US) accounted for nearly 80% of the entire imports and exports of the US and employed around 20% of the entire US workforce (see Bernard et al. 2009 for figures for 1995-2000 period).

Unsurprisingly, the prominence of MNCs in the global economy has spawned a growing literature that focus on a number of dimensions regarding the role of firms in international trade. Empirical studies that follow the seminal work of Melitz (2003) have been treating firms as the central unit of analysis and examine their asymmetrical gains from trade opening (e.g. Ramondo et al. 2013; Baccini et al. 2018).[1] Others that take a political economy approach have been attempting to better understand firms' lobbying patterns and influence over economic policies (e.g. Jensen et al. 2017; Kim et al. 2018) In addition, theoretical work has been conducted to better grasp firms' governance of value chains (e.g. Gereffi et. al. 2009) and the difficulties surrounding the regulatory governance of MNCs (e.g. Ruggie 2018).

Yet, despite their quality, scholars have so far looked over the ability of MNCs to operate across value chains to achieve political goals – i.e. MNCs as coordinators of political activity in networks that they develop and operate within. Indeed, the business literature has long been demonstrating the ways in which firms organize their foreign operations (e.g. Arndt and Kierzkowski 2001; Williamson 1975), and recent work on GVCs have been focusing on firms' governance of global production networks (e.g. Gereffi et al. 2005; Fung et al. 2007). Despite their quality, however, scholars have emphasized the rational-economic behavior of MNCs without focusing on their political behavior. These studies commonly rely on economic and organizational theory to emphasize firms' economic or production-related decisions. Interest group scholars have been complementing these analyses with firm-level lobbying studies (e.g. Osgood et. al. 2016) borrowing from heterogeneous firms theory (e.g. Plouffe 2015) and building on a long line of work conducted by international political economy scholars (e.g. Milner 1995). Yet, even scholars who focus on MNCs political behavior ignore the coordination of political activity undertaken by MNCs along their networks and treat them as unitary actors that pursue political goals on their own.

[1] e.g. See Antras and Yeaple 2015 for an overview.

Given their outsized role in the global economy, MNCs coordination of political activity remains as an important gap in these literatures.

Consider the multi-jurisdictional political activity of one of world's largest producers of food condiments, a Japanese MNC named Ajinomoto, along with its subsidiaries in the European Union (EU) and the US. Ajinomoto is credited as the first (and possibly the largest) producer of monosodium glutamate (MSG) that is found in a variety of foods including soy sauce. The company commands over thousands of employees and operates in 30 countries worldwide with a revenue of over 1 trillion Japanese yen in 2016.[2] In January 2015, the subsidiary of this MNC, Ajinomoto Foods Europe, based outside of Paris, obtained trade protection from the European Commission in the form of roughly 30-40% import barriers.[3] The import tariffs affected around EUR 50 million worth of exports of MSG between 2014 and 2015 and were imposed on Indonesia and China, the two largest exporters of the product into the EU.[4] Around the same time, Ajinomoto North America, which, as the name suggests, is another subsidiary of Ajinomoto, also obtained similar protective barriers against Chinese and Indonesian firms that export into the US.[5] In other words, a global company coordinated the raising of barriers through its subsidiaries levied on Indonesian and Chinese exports to the EU as well as the US at the same time. Ajinomoto was subject to AD duties itself in Europe in 1998, without affiliated enterprises operating in the EU. The producer of MSG of the time, Orsan S.A. Limited, obtained protection in 1998 from the European Union[6] and it was acquired by Ajinomoto 4 years later.[7]

Similar to Ajinomoto, highly-resourceful MNCs use their global reach to keep out competition from different markets in which they operate through their subsidiaries and affiliates. Thanks to their global

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[2] Ajinomoto Global Financial Report. Accessed on 21 March 2017 via https://www.ajinomoto.com/en/ir/library/annual/main/01/teaserItems2/0/link/Aji_FR2015_E.pdf.

[3] Values of exports to the EU of MSG, which fall under TARIC code 292242, was reported to be USD 66.3 million in 2014 and decreased to USD 43.6 million in 2015 – presumably because of the anti-dumping restrictions. The values can be calculated from UN COMTRADE.

[4] See, Official Journal of the European Union 2015 L15/31, *COMMISSION IMPLEMENTING REGULATION (EU) 2015/83 of 21 January 2015, imposing a definitive anti-dumping duty on imports of monosodium glutamate originating in the People's Republic of China following an expiry review pursuant to Article 11(2) of Council Regulation (EC) No 1225/2009* and Official Journal of the European Union 2015 L15/54, *COMMISSION IMPLEMENTING REGULATION (EU) 2015/84 of 21 January 2015 imposing a definitive anti-dumping duty and collecting definitively the provisional duty imposed on imports of monosodium glutamate originating in Indonesia.*

[5] See: US International Trade Administration 2015, Monosodium Glutamate From the People's Republic of China: Preliminary Results of the Antidumping Duty Administrative Review; 2014-2015, accessed on 21 March 2017 via: https://www.federalregister.gov/documents/2016/08/05/2016-18669/monosodium-glutamate-from-the-peoples-republic-of-china-preliminary-results-of-the-antidumping-duty.

[6] See, Official Journal of the European Union 1998 L264/1, *COUNCIL REGULATION (EC) No 2051/98 of 24 September 1998 imposing a definitive anti-dumping duty on imports of monosodium glutamate originating in Brazil and Vietnam, amending Regulation (EC) No 81/96 in respect of anti-dumping measures concerning imports of monosodium glutamate originating in the Republic of Korea and Taiwan and terminating the proceeding in respect of imports of monosodium glutamate originating in the United States of America and Indonesia.*

[7] Tate and Lyle 2002 Press Release, Tate & Lyle PLC: Conditional sale of monosodium glutamate unit to Ajinomoto, accessed on March 21, 2018 via: https://www.tateandlyle.com/news/tate-lyle-plc-conditional-sale-monosodium-glutamate-unit-ajinomoto.

integration strategies, multinational firms are able to coordinate mobilization over trade policy objectives in different markets and capitalize on their global trade network to reach their political goals.

In order to better understand role of MNCs in the global economy and to examine their political behavior, this article lays out a framework by building on three streams of the literature; heterogeneous firms (e.g. Madeira 2016), global value chains (e.g. Gereffi et al. 2014), and governance (e.g. Abbott et al 2018). Building on the assumption that firms are the main political actors in trade governance, I put forward that MNCs engage in political activity in different jurisdictions simultaneously by working with affiliates and subsidiaries in their network. Following the fragmented nature of their production networks, firms have various forms of relationships with other enterprises, ranging from full ownership to strategic alliances. Depending on the flexibility of their affiliation with firms in their networks, MNCs directly delegate political activity to their subsidiaries or orchestrate the political mobilization of their affiliates in search of political goals. They engage in such costly coordination either because they seek legal standing in markets they are treated as foreign producers, or because they seek to increase their political clout by cultivating a critical mass. In the end, these global political-economic actors engage in costly coordination to increase market shares, profits, and limit competition.

This article thus provides a conceptual lens to look at MNCs not only as a single unitary actor but also as a coordinator. In order to do so, it first outlines how MNCs are able to exercise coordination and through which models. Then, it provides an account of why firms engage in such costly behavior. It concludes with the broader relevance of its propositions. Overall, the article will serve as a useful companion to political scientists, economists, and international law scholars who want to examine the behavior of multinational enterprises in reaching their trade policy objectives and to better understand their role in economic governance.

Coordination and Governance

In order to unpack the features of MNC coordination of political activity, I build on three streams of literature. I start by building on the growing literature on heterogeneous firms and trade politics that broadly highlights firms as the primary political actors (e.g. Madeira 2016), rather than sectors or factors of production. Scholars working in this literature have shown the extent to which MNCs have extensive resources to undertake costly political activity (e.g. Milner 1995) often 'alone' and not along sectoral lines (e.g. Osgood 2017) and have multidimensional trade policy objectives (e.g. Kim et al. 2018). Such 'super star' firms are often the ones that build, deepen, and develop production networks, and their trade policy preferences are naturally complex. For one, the location of their economic activity has implications for their preferences in a given market – such as raising of trade barriers against their competitors in a given country while lobbying for a trade agreement in another. Even though we might often assume MNCs to be the main drivers of trade liberalization across the board – as they are often portrayed – they often lobby for contingent trade protection (Bown 2005). Therefore, unsurprisingly, MNCs often pursue *separate policy objectives* based on the location of their supply chains or their foreign investment.

Take the automotive producers in the US for instance. While the largest car producers in the US have been great supporters of free trade agreements overall, in mid-2000s they lobbied to actually withdraw the US from a sector-wide trade agreement named *US-Canada Auto Pact*, which had been in place since the 1960s. The reason was that this sector-wide trade agreement was found to be inconsistent with World Trade Organization rules in 2002 and instead of allowing other countries to join in, the Big Three (GM, Ford, and Chyrsler) lobbied for the dismantling of the Auto Pact to avoid leveling the playing field with their competitors in the North American automobile market (Krikorian 2005).

Beyond separate policy objectives, we know that firms coordinate their production networks through different types of value chains (Gereffi et al. 2005:84). Large in parts thanks to the insights generated by the scholarship on GVCs, MNCs' coordination of their value chain activities is well-understood. Scholars have noted that MNCs often keep the core competencies of their expertise in-house, outsource the labor-intensive parts of their production abroad, and that they help firms in their network adopt standards (Yeats 2001; Feenstra 1998). In turn, they streamline their operations and lower transaction costs of co-producing with firms in their networks, ultimately lowering production costs and maximizing profits (Fine 1998).

Following this literature, I propose that firms' coordination of economic activity regarding their production also serves as an opportunity for them to coordinate political activity. Having fragmented parts (or the entirety) of their production abroad (e.g. Helpman et al. 2009), MNCs engage in at least three types of internationalization: 'vertical integration', where firms take ownership of their supply chain partners and internalize production processes; arm's length trade with independent suppliers, where MNCs engage in strategic alliances with other enterprises they work with; and, lastly, horizontal integration (sometimes titled 'horizontal investment') through which global firms replicate their activities in different economies and establish independent entities in different regions.

The differences in the type of internationalization MNCs partake in has implications for the different forms of relationship they have with firms they are associated with. From a legal perspective, different corporate entities across value chains, even in the same corporate group, are considered independent entities and operate in a legally fragmented regime (Leader 2017). This fragmentation has its advantages from the perspective of the firm, namely that the headquarter is often not considered responsible for the practices of its partners down the chain – limiting the potential adverse consequences of mass production for instance (Ruggie 2013). In practice, MNCs operate with various degrees of ownership with peer enterprises along their value chains, which ranges from full ownership to strategic alliances. In turn, if and when a firm is after a policy objective, it has to resort to different models of governance to maximize its chances of achieving its goal and coordinate the political activity of their group members.

Thus, MNCs' choice of a particular governance model rests on the form of relationship they have with other enterprises in their network – i.e. whether or not they operate through fixed relationships with firms in their network through ownership or through more flexible arrangements without ownership, such as strategic alliances.

Here I borrow from the governance literature and apply it to inter-firm relationships. I put forward that MNCs' activity includes a mix of two logics of governance, i.e. governance through delegation of political activity or through orchestration. Following the principal-agent (P-A) theory (Hawkins et al. 2006), a cursory look can identify MNCs as principals and their subsidiaries and affiliates as agents. This would be broadly in line with P-A governance models where an actor, *in casu* an MNC, who wants to reach a political objective, delegates activity to an agent, e.g. a subsidiary. MNCs sit at the top of a hierarchy and have stakes in different enterprises across various countries – often across continents. Given their economic power and how much affiliates would depend on them for their survival, a first look at MNCs' political mobilization of affiliates along trade networks would yield a P-A model ideal. This is because the ability of an headquarter to exercise hard control is clear, along with its ability to grant authority for a particular policy action – such as an anti-dumping petition. Above-mentioned example on the Japanese MNC Ajinomoto's behavior would be an example of this.

Yet, such cases are "easy" ones involving MNCs and wholly-owned subsidiaries. In practice, MNCs often do not actually own their supply chain partners, and work with firms within their own networks with limited or no ownership. MNCs work with highly specialized suppliers who cannot be easily substituted, giving these (often smaller) firms substantial power and creating an interdependent relationship rather than a hierarchy. In other cases, firms' supply chain partners are partially owned. This variation in the form of relationship MNCs have with associated firms clouds the potential clarity of applying a P-A model to inter-firm relationships. The primary reason is that the ability of the principal to punish its agent in cases of non-alignment is unclear if an MNC does not own its partner and is unable to perform hard control.

Indeed, some firms do not own *any* of their partners but only coordinate supply chain networks. Li and Fung, a global apparel giant, is a good example of this. Without a single factory, this MNC indirectly employs thousands of workers and collaborates with thousands of firms based on the orders it receives from its customers (Fung et al. 2014). Examining such a firm and its network would be much more suitable with a model of orchestration (e.g. Abbott et al. 2015). In such cases the targets, i.e. policymakers, would be approached by intermediary firms, i.e. affiliates that are ultimately coordinated by MNCs. Both actors in such situations have common goals of survival, profit maximization, and limiting competition. MNCs then act as orchestrators to help achieve goals of their partners that ultimately help them as well.

A possible example of such coordination could arguably be observed when pharmaceutical companies were vehemently supporting the adoption and the implementation of Canadian European Comprehensive Economic and Trade Agreement (CETA) with their affiliates and subsidiaries. Global pharmaceutical giant Johnson and Johnson (J&J) for instance, appeared before the Canadian government (both directly[8] and through the pharmaceutical sector association Innovative Medicines Canada[9]). It also lobbied the European Commission through in-house lobbyists as well as through external consultants[10]. J&J's parent company Janssen simultaneously engaged in lobbying in Canada, while J&Js suppliers such as Merck Group also reported lobbying for CETA.[11] Similarly, Novartis and its affiliate Sandoz Canada both lobbied for CETA at the same time.[12] [13]

As MNCs have varying relationships with different enterprises in their networks, I propose that a mix of delegation and an orchestration approach is needed to better understand their behavior. A given firm in a given moment has above-mentioned forms of relationship simultaneously. Consider the French gas giant Total. The company works with over three thousand associated firms, wholly owns only a handful of them, and has joint investments with over a thousand firms in its network (Ruggie 2018). This indicates how different Total's relationship is with the firms in its network. Therefore, a useful approach to examining MNCs' political activity would be to unpack the conditions under which these highly powerful global actors can apply a particular type of governance strategy with a given partner.

In cases where MNCs engage in vertical integration and take ownership of their partners, they are more likely to exercise a principal-agent type of direct (hard) control over their intermediaries to reach their

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[8] See, for instance, *Proceedings of the Standing Senate Committee on Foreign Affairs and International Trade of Canada*, Issue No. 22, Meeting of April 12-13, 2017. Accessed on 10 November 2019 via https://sencanada.ca/en/Content/SEN/Committee/421/aefa/22ev-53252-e

[9] Innovative Medicines Canada Statement on the Implementation of CETA. Accessed on 10 November 2019 via http://innovativemedicines.ca/statement-implementation-of-ceta/

[10] See Corporate Europe 2015, *Policy Prescriptions: The firepower of the EU pharmaceutical lobby and implications for public health*, accessed on 10 November 2019 via https://corporateeurope.org/sites/default/files/20150904_bigpharma_web.pdf

[11] For Janssen's lobbying activity, see: Office of the Commissioner of Lobbying of Canada, accessed on 10 November 2019 via https://lobbycanada.gc.ca/app/secure/ocl/lrs/do/clntSmmry?clientOrgCorpNumber=14483&sMdKy=1427394309976 For the lobbying activity of Merck Canada, see: https://lobbycanada.gc.ca/app/secure/ocl/lrs/do/vwRg?cno=12241&regId=863379

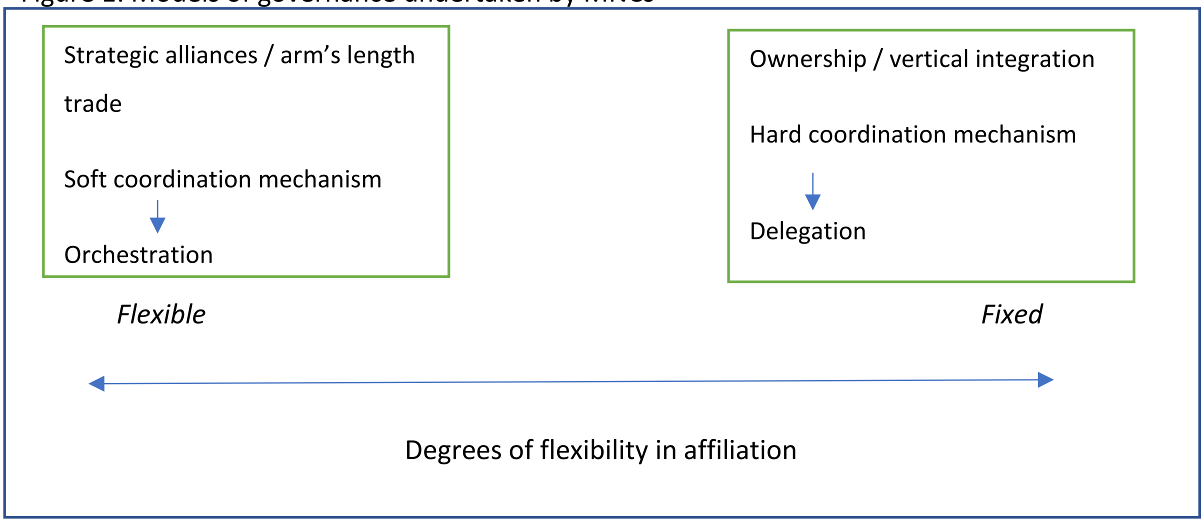
[12] See: Office of the Commissioner of Lobbying of Canada, accessed on 10 November 2019 via https://lobbycanada.gc.ca/app/secure/ocl/lrs/do/vwRg?cno=15599&regId=863635 and for Sandoz Canada, https://lobbycanada.gc.ca/app/secure/ocl/lrs/do/vwRg?cno=234283&regId=858340

[13] Clearly, these companies might have had independent interests in CETA and could have been lobbying by themselves without the involvement of their headquarter firms. This would be observationally equivalent to MNC coordination of political activity. This critical problem can only be solved by further scholarly work, potentially with in-depth studies – a point I return to in the conclusion.

political goals. Fragmenting their operations in such a way give multinationals an opportunity to compartmentalize their trade policy preferences in different markets and mobilize politically using their in-house subsidiaries, allowing them to control their intermediaries with relative ease. On the other hand, MNCs are more likely to exercise orchestration and engage in more indirect soft(er) coordination if they work with arm's length suppliers or through affiliates where they have less than majority ownership. In such cases, MNCs share similar governance goals with their partners but operate in a limited hierarchy. While MNCs and their affiliates work closely and share political objectives, MNCs have much less direct capacity for hard control and hence less likely to exercise delegation.

Another way to look at this would be to treat full ownership and the independent supplier relationship (e.g. arm's length trade) as the two ends of a continuum in which MNCs' relationship with each firm is located somewhere between the two ends. Therefore, the level of flexibility in an MNC's relationship with its network partners has an important implication on its governance options. While fixed affiliations that are typical of ownership relationships would result in delegation, more flexible relationships such as strategic alliances would be better understood through orchestration – I outline this framework below on Figure 1.

Figure 1: Models of governance undertaken by MNCs



Firms' incentives

What is the advantage for an MNC to coordinate political activity, rather than acting itself? Do MNCs benefit from exercising costly coordination activities through their networks? Similarly, what is the advantage for an affiliate to politically mobilize along with its larger partner, instead of lobbying by itself?

The answer depends on whether or not the headquartered MNC is a 'foreign' one or a 'domestic' one.[14] For a foreign MNC, the incentives are twofold. First and foremost, having affiliates in a country allows a

[14] I use quotation marks here to indicate that MNCs could be headquartered in a country and be able to serve an economic area, such as the European Union. In this sense, a foreign MNC would be an extra-regional one.

foreign firm to buy standing from local authorities, i.e. in markets where they would otherwise be treated as a 'foreign producer'. This is especially the case for anti-dumping petitions (Messerlin 1996). Instead of being treated as foreign firms, and thus unable to petition for anti-dumping protection, MNCs can buy legal standing through ownership of supply chain partners. While all multinationals have a similar incentive to seek profits and limit competition, operating with independent suppliers will not give firms legal standing to apply for protectionist trade barriers from local authorities. On the other hand, if and when MNCs operate through ownership with their partners, they are able to use their subsidiaries in local markets to seek protection that ultimately benefits their operations – raising trade barriers for their competitors. For instance, following the example given above on the political activity of Japanese MNC Ajinomoto, acting through a subsidiary allowed it to act as a vulnerable local company that needed protective measures against unfair foreign competitors. Thus, MNCs can use their subsidiaries and fulfill legal requirements in different markets in order to achieve their political objectives.

For domestic MNCs, their incentive to coordinate political activity is influence by two reasons. One, MNCs that govern a network of suppliers, affiliates, and subsidiaries are able to create a sort of critical mass. By mobilizing together with their subsidiaries and affiliates, these firms are able to increase their leverage over policymakers and better consolidate their resources to reach political goals. In other words, MNCs may be able to increase the number of domestic actors that seek a particular goal and align a constellation of interests for coordinated lobbying. Second, MNCs may be able to mask potentially unpopular decisions behind their partners' actions. For instance, last year a small subsidiary of a Finnish MNC called Afarak Group PLC petitioned for temporary trade protection from the EU against exports of Turkish, Chinese, and Russian intermediate steel products.[15] In this case the Finnish MNCs' use of its smaller partner to impose costs on its competitors was extremely convenient. It turns out, Afarak had been acquiring extraction firms in Turkey and have been waiting for drilling licenses across the country. It is likely that the Turkish government would have been displeased if its new investor is acting bluntly against domestic Turkish firms in the EU.

For the affiliates (or subsidiaries) of global firms, the incentives for political action is twofold. For one, their chances to undertake costly political activity are much higher if they become parts of larger companies. MNCs can support their partners through legal and economic resources to undertake political activity – e.g. lobbying. While smaller enterprises often do not have the necessary resources, staff, or skills to conduct political activity, MNCs can provide them with tools to achieve their shared political goals. Second, affiliates are often empowered as parts of MNC networks. Larger corporations allow their

[15] See, Official Journal of the European Union 2017 C200/17, *Notice of initiation of an anti-dumping proceeding concerning imports of Low Carbon Ferro-Chrome originating in the People's Republic of China, Russia and Turkey.* The company that petitioned was called Elektrwerk Weisweiler (EWW) GmbH but it's a wholly-owned subsidiary of Afarak Group PLC.

network partners to access know-how, grant them licenses, and support them through training. This further consolidates their goals' alignment with that of their larger partner. All in all, (often smaller) MNC partners' political goals are more likely to be pursued when and if they are parts of larger corporate networks.

Concluding remarks

In this article I have outlined a conceptual framework to examine the behavior of multinational enterprises that sit at the center of the global economy. I have proposed that analyses of MNCs needs to incorporate their political activity as coordinators within a network where they are able to govern through different models. Depending on their form of relationship with enterprises in their network, MNCs are likely to delegate political activity to their subsidiaries or orchestrate intermediary firms to reach political goals. Their incentives to do so is shaped by their inability to have legal standing in certain jurisdictions or to cultivate a sort of critical mass and increase the number of actors mobilizing in favor of a certain policy position.

While anecdotal evidence given above is indicative of MNCs' political behavior, more rigorous studies are needed to shed light on MNC coordination of political mobilization. Future studies will have to undertake the difficult task of untangling firms' political behavior as either independent or through MNC coordination. While large-n firm-level studies can identify patterns of MNC-affiliate behavior, more in-depth analyses can shed light on firms' incentives and the extent to which subsidiaries or affiliates were under explicit governance of their MNC partners.

This framework is an ideal starting point for further firm-level analyses. It will serve as a useful companion to at least three strands of literature; the international political economy scholarship that focuses on trade and globalization, the literature that examines different model of governance in international relations, and the international law scholarship that focuses on the role of MNCs and cross-border regulations. While the growing IPE literature on international trade has so far tackled important questions such as the distributive consequences of trade agreements and the impact of internationalization of production, analyses of the political activity of global corporations in shaping the domestic political economy of trade policymaking have yet to receive scholarly attention. Similarly, the growing amount of studies that examine governance through orchestration and delegation has yet to focus on the activity of private economic actors as governors. Lastly, the framework I set out will also benefit the international law literature on MNCs that highlight the governance gap on regulating the activity of these firms. I note that governance of economic activity should be seen in tandem with governance of political activity, stemming from growing fragmentation of production and equally fragmented legal regimes.

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