because it needs relatively less assistance from host governments in terms of information, it pays less attention to minor administrative problems and normal business risk, to differences in laws and regulations and even to political instability. It is, on the other hand, more difficult precisely because it can choose another site, play off one government against another, and, for 'foot-loose' firms, scan the countries for fiscal incentives.

145. The distinction cannot be pushed too far, but it may be safe to generalise that the greater the economic attraction of a country (in terms of its market and the entry of competing oligopolist's) the less will the factors mentioned above affect the investment decision of the MNC, while the smaller the economic attraction of a country the more will they become relevant. Furthermore, the smaller foreign investor will generally require more wooing by the host government but may be able to affect the terms of its entry less, while the multinational may require less wooing but will be able to impose more rigorous terms on the government.

146. The attraction of foreign capital is, however, not the only problem facing host governments. We have argued that the pervasive nature of MNCs requires action by host governments at various levels; some of these could deliberately restrict the scope of MNCs' entry and operations, while others may unintentionally deter otherwise desirable foreign investment. If the 'rules of the game' were, however, worked out in sufficient detail and implemented efficiently, it is likely that the amount of desirable MNC investment would not be too adversely affected over the long-run. Certainly the final result would be better than the patchwork of restrictionist and encouraging policies which are being built up now, on an ad hoc basis under pressure from various forces, without a clear idea of what factors are involved and what end is to be achieved. Let us, therefore, consider the requirements of policies of regulation and control and try and construct a more coherent structure.

CHAPTER V MNCs AND POLICY ISSUES : evaluation, control and bargaining

147. It will be helpful at this stage to revert to the distinction between the four 'levels' at which MNC effects were discussed (in Chapter III). The taxonomy is mainly for analytical purposes. It is not suggested that the policy issues at each 'level' should be clearly demarcated and handled by different administrative units; on the contrary, it will be recommended that dealings with MNCs should, with obvious exceptions of issues which can only be dealt with on a national scale, be entrusted to a centralised body and not spread over various departments. Furthermore, a number of issues, mainly concerning technology, the composition of output, ownership and income distribution, form a common thread which runs through all the 'levels'; the distinctions made below are, in consequence, bound to be somewhat arbitrary. Bearing these points in mind, let us proceed with the argument.

The General Level

It is at the general level of the social, cultural, political and economic life of a country that the effects of MNCs, and of foreign influence in general, are most difficult to discern and deal with. While it can hardly be denied that such factors do exist and interact between different countries, it can certainly be argued that such 'interdependence' (to distinguish it from the 'dependence' case) is a necessary fact of modern life, and even that it is a desirable and efficient method of promoting the 'modernisation' and 'development' of the power countries(1). These words (in quotation marks) have extremely vague meanings; usually they mean what the user, like Humpty Dumpty, wants them to mean. We have proposed that development does not imply a wholesale importation of the consumption, production and distribution patterns of the developed capitalist countries, as is inherent in the opening up of developing economies to the developed ones by means of foreign investment and free trade. While 'interdependence' may certainly exist, and the influence of socio-political-economic factors may work both ways, we agree with the dependence school that the influence is heavily asymmetrical: developed countries have a much larger effect on the pattern of development in less-developed ones than vice versa, and that the result is not one which promotes the welfare of the majority of people there.

149. It is difficult to say whether or not such influence is 'necessary'. It is necessary if the host developing country wanted to follow the dependent pattern; it may, to some extent, be avoided of a different pattern of development were envisaged. Certainly some of the ill-effects can be mitigated by appropriate policy, and we shall discuss these rather than go into extreme solutions of armed revolution.

150. The most important issue is the inter-related one of income distribution and composition of output. If distribution is very uneven, and the structure of production is geared to it, the entry to MNCs on a large scale will tend to bias consumption even further towards the elite, and to create pressures in favour of policies which promoted a preservation and accentration of inequality. This issue is much broader than one simply of foreign investment, and a real solution may well involve extreme measures; however, within the constraints of a given socio-political structure, the government can undertake the following measures to reduce the impact:

(i) Sectoral control of MNC entry, restricting it to industries where its output is considered socially beneficial. Needless to say, industries which are socially undesirable should not be promoted with local enterprise; nor should their products be freely imported. We cannot go into precisely what is desirable for each country; much depends on the levels of income, social norms and cultural requirements - though these are also subject to change.

(ii) The promotion of income equality through fiscal measures, and by use of appropriate technology (see below). These considerations may well permit MNC investment in export industries regardless of the composition of output, if other factors were favourable.

151. The issue of technology is also significant at the general level, and concerns both national science and education

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(1) For a clear exposition of the 'dependence' case, see Sunkel, 1969-70, and for a sympathetic critique see O'Brien, 1974.

policy as well as the choice of techniques used. (1) The basic problem is to stimulate local research and development in order to build up the (cumulative) capacity to innovate and to adapt technology to local needs, without wasting resources in reproducing work already done abroad and without committing avoidable mistakes. A passive and total dependence on MNC technology would stifle local innovation, use capital-intensive techniques, and so, even in socially desirable industries, promote income inequality. Possible measures to deal with these problems are:

(i) To set up and actively promote research centres in the public sector to adapt foreign technology to local needs, both in terms of the type of output and the use of inputs.

(ii) To induce local firms buying foreign technology to become independent of imported techniques, to invest in adaptive R and D, and to use the results of local innovation as far as possible.

(iii) To induce small foreign firms to invest (or to sell technology) using techniques which are more labour intensive and perhaps use locally available skills, and producing goods which are not the most 'modern' but more sensible for the host country. This may reduce the cost of capital goods imports by utilising second-hand equipment, and simultaneously reduce the scope for rapid product-differentiation.

(iv) To induce MNCs to adapt their technology to local factor endowments(2), by correcting relative factor prices as far as possible, by contracting with them for the development of specific technologies, by specifying a certain amount of local R and D, and by restricting their entry into sectors where local technology was considered inadequate.

(v) To induce foreign private or public international organisations to undertake the requisite adaptive R and D and the development of intermediate technologies, and to diffuse the knowledge of such innovations in one developing country to all others.

(vi) To promote cooperative, regional or other, research between different developing countries facing similar technological problems.

152. The issues of political pressure is more difficult to deal with, simply because government policies are themselves an outcome of conflicting internal and external pressures, both of which are in turn affected by MNCs. By external pressures we mean pressures from abroad (by the home governments and international organisations)(3) and from national groups outside the government (local businessmen, professionals, traders, etc): by internal pressures we mean the influence of groups within the government and the administration supporting the MNC cause. Insofar as the

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(1) On the problems of national science & education policy, see Sunkel, 1971.

(2) See Helleiner, 1974.

(3) Hayter, 1971, presents a critical examination of such pressures from aid donors.

policy-making and implementing process must be shaped by these pressures, the only way to minimise them is to limit the scope and total amount of foreign capital in the country, and to foster attitudes which reduce intellectual social and political 'satellisation'. This again raises broad issues of aid and trade relations, education policy, income distribution, the role allotted to the public sector, and so on, all of which fall outside the scope of our paper yet are directly related with it.

153. The issue of local entrepreneurship is ambiguous, in that it has been argued that MNCs both supress local enterprise and promote it. Perhaps the two are not incompatible: MNCs can take over the leadership of the most dynamic technological industries in which their main advantage lies, thus suppressing local initiative, while promoting the expansion of local ancillary industries, thus stimulating it. The net effect is not clear; what is likely is that local enterprise is reduced permanently to a secondary role and that all the major initiative in indsutrial development passes to foreign enterprises. If this is regarded as undesirable for other reasons, the answer is to:

(i) Reduce the extent and scope of MNC entry;

(ii) Restrict it to sectors where local enterprise is lacking, or to where its technology is necessary;

(iii) Restrict its ownership and control by promoting joint ventures, subjecy to the MNCs bargaining power and to the qualification that this may not prevent the suppression of weak local entrepreneurship but merely ensure it a share of the MNCs quasi-rents;

(iv) Restrict its activities and ownership over time by having 'divestment' arrangements(1). Such provisions have now been incorporated into the rules of the Andean Pact.

154. Many such policies are already in force in a number of developing countries; India, for instance, issues periodic lists of industries in which foreign investment is allowed, in which foreign technology but not direct investment is allowed, and in which neither is allowed. The rationale of such policies may be seen as the breaking up of the foreign investment 'package' into its components, and of finding a compromise between the facts that its entrepreneurial and organisational contributions are harmful while its technological contributions are beneficial.

The Sectoral Level

Once the desirable amount and pattern of foreign investment has been decided, the problems which arise at the industrial level concern product differentiation, marketing methods, technology, access to capital, organisational and productive efficiency and relationship to suppliers. Some, especially technology and effects on local entrepreneurship have been mentioned above and need not be discussed again till later.

156. The problems of MNC marketing and product differentiation are related partly to income distribution and the composition of output, which we have discussed already, and partly to their effects on the practices of other firms in the relevant

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(1) See Hirschman, 1969, for proposals for setting up formal divestment arrangements in Latin America.

industries. If the effect of MNC entry is to change marketing practices so that advertising expenditures rise for the sector as a whole and oligopolistic product differentiation and rapid model changes become much more common, there is a social cost involved which must be reduced by government action:

(i) Advertising tactics and expenditures can be regulated by special consumer protection bodies, similar in concept to the institutions recently set up in the United Kingdom. The social value of advertising in terms of its informational content, must be weighed against its costs, such as its distortionary effects on consumption of people with low incomes, or its confusion of true market information (which can be important in industries like pharmaceuticals). There is some conflict between the roles of advertising as a means of healthy competition and as an instrument for moulding tastes or promoting unnecessary consumption; the correct method of regulation can only be found by trial and error.

(ii) Product differentiation and model changes can be controlled by laying down specific criteria for permitting the introduction of 'new' products, comparing their performance with existing ones and judging their social desirability. There are, once more, problems of deciding how far minor modifications add to performance, and how far competition in this manner is necessary for productive efficiency. Clearly the extent to which such practices exist in developed nations is not recommended for poor countries, but clearly products (especially in non-consumer goods industries) also improve over time in some objective sense, and some compromise has to be found between the two.

157. The access to capital of local enterprises may be limited by MNC entry if financial institutions and capital markets give preference to the larger foreign enterprises than to smaller national ones. This problem may be exacerbated by the entry of foreign banks and other financial institutions. To some extent the preference may simply reflect 'sound' banking practice, but it may also deprive 'sound' local borrowers of scarce capital and may be influenced by an irrational bias in favour of established names. To counter this, the government may:

(i) Limit the amount of long-term local borrowing of MNCs;

(ii) Induce then to accept local capital in the form of equity rather than loans;

(iii) Induce financial institutions to lend to local enterprises by guaranteeing these loans, or by laying down statutory provisions;

(iv) Counteract the irrationality of capital markets by itself holding local shares, or namaging unit trusts with properly balanced portfolios;

(v) Assist local enterprises directly by lending from state funds.

158. The issues raised by productive efficiency, market concentration, relationship with suppliers, and so on may be dealt

with together as the general effect of MNCs on the productivity of the industry. We have noted that this effect may well be favourable if their entry destroys local monopoly, induces changes in organisational and productive methods and develops local supplies. The basic problem with trying to protect local enterprises lies in the danger that the government may end up subsidising inefficient production for inexcusably long periods, and may delay the introduction of necessary changes in their structure. As with determining any sort of protectionist policy, one has to find the correct balance between inefficiency and suppression of viable entrepreneurship.

159. To maximise the benefits of MNCs in these respects and to prevent the emergence of concentration in the MNCs' favour, the government may:

(i) Pass and implement anti-monopoly legislation, controlling take-overs and preventing predatory action on the part of any firm, foreign or local. This may include the regulation of retail prices, control of retail outlets, franchises, and so on;

(ii) Specify the local content of inputs used by MNCs, in order to promote local suppliers but not at too high a cost in terms of protection.

(iii) Regulate wage and employment policies of all the firms, ensuring, on the one hand, that they all observe minimum wage and social security requirements, and, on the other, provide training to their employees.

The Project Evaluation Level

We have little to add to what has already been said above about decising upon the social desirability of projects(1), except to reiterate that market prices are not a reliable guide, and considerable judgement, rather than a set of automatic rules, has to be exercised in selecting worthwhile investments. Once the desirability of an investment is established, taking into account its competitiveness in international terms (the level of protection and costs of imports may themselves be subject to bargaining, discussed below), such 'externalities' as its effects on training, skills, learning by doing, and the environment, and its technology, the problem arises of deciding whether or not it can be undertaken by local enterprise.

161. The comparison of local and foreign enterprise is hazardous and based on many imponderables. In particular, it must take into account such items as the shadow price (opportunity cost in social terms) of local capital, the capacities of local entrepreneurs, the availability of technology either locally or abroad without foreign direct investment, the ability of local enterprises to export, and their effects on employment and training. In terms of concrete policy, the project evaluation exercise requires the establishment of a unit which possesses comprehensive information on technology and foreign markets, has extensive contacts with local enterprise, and has the ability to select projects along lines which promote social welfare. It must also have close contacts with the unit which bargains with MNCs, or it could be a part of the same unit, since the choice of foreign or local ownership must be made simultaneously with the decision to undertake a project.

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(1) For recent advances in project evaluation see Little and Mirrlees, 1974, and UNIDO, 1972.

162. The main dangers which policy makers must guard against at this level are:

(i) They must not have recourse to rigid and over-simplified rules in selecting desirable investments.

(ii) They must not be swayed by pressures exerted by particular groups, either local or foreign, to override considerations of broad, social and national welfare.

(iii) They must not take a narrow view of technology and accept whatever is offered, but must bear in mind its appropriatness, adaptability, local availability and cost; at the same time, however, they must not fall into the trap of taking a static view, assuming that once a particular technology is present locally nothing more need be done to keep up with innovation abroad. A number of proposals for divestment and technology purchases tend to ignore the dynamic aspect of technology, and the fact that continuous contact has to be maintained in some cases to gain the maximum benefit from it.

163. It may be worth emphasising that the problems of valuation raised in the early parts of this paper are very difficult ones, which do not admit to easy, straightforward solutions in theoretical or practical terms. While it is only natural that social welfare is an elusive and complex concept, open to many interpretations, it is something which has to be defined, albeit crudely, for the pressing needs of day-to-day policy making, and acted upon by numerous people in the government and outside. We have not sought to pursue the definition in any depth, using the economist's usual escape route of leaving it to 'the policy maker'; however, we realize that the policy maker is neither independent of pressures nor ominiscient, and that leaving decisions to the arbitrary judgement of officials raises all sorts of difficulties of its own. We shall return to these questions in the final section.

Bargaining

The real spadework of dealing with foreign investors and MNCs has to be done at the level of bargaining and regulation. The potential benefits of astute bargaining to the host country are now co-monly accepted in the literature, and the tools of game theory are often used to illustrate the complicated and fundamentally indeterminate nature of the process and its outcome. The question of bargaining in this context arises because there is no well-structured competitive market for foreign investment or for its various componenets, and the range within which the 'prices' set can lie is very broad indeed.(1)

165. The bargaining strength of the respective parties, MNCs and host countries, lies in the benefits they offer to each other and the costs of comparable alternatives. The benefits offered by MNCs consist of their capital, technology, management, access to overseas markets, provision of special inputs, marketing know-how, and contacts with foreign governments and financial institutions:(2) the alternatives to

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(1) See Streeten, 1973, and Kindleberger, 1969.

(2) These are benefits defined in a commercial sense; clearly not all of them are valuable, even desirable, for the social welfare of the host country.

investment by a particular MNC are investment by another MNC, the purchase abroad of technology, managerial talents or other scarce components of the package by a local investor (public or private), the local provision of all the components, import of the relevant products, or doing without these products altogether. The benefits offered by host countries consist of their market, labour, natural resources, infrastructure, and sometimes technology; the alternative to investment in a particular country are investment in another country with comparable benefits, selling components of the package to a local enterprise, or withholding investment altogether (and trying to export to it from abroad).

166. Given the basic bargaining positions of the two parties, there are various elements of strategy which can modify the process and its coutcome. The provision of concealment of information about costs and benefits, and about future action, is perhaps the most important. In any bargaining position, both parties try to make their position appear as strong as possible, and take recourse to various tactics like threats, bribes, concessions, and even walk-outs to wear down the other. It can plausibly be argued that, apart from the objective benefit - and alternatives - situation and the ultimate power of a national government to expropriate, it is the MNCs which possess the upper hand in bargaining strategy. This is so for a number of reasons:

(i) They are often the sole possessors of particular pieces of advanced technology, which the host government cannot hope to imitate for reasonable costs.

(ii) Even of the technology is not unique to them, the host country is often unaware of alternative sources, and is unable to assess the real value of the technology.(1) The same problem arises for assessing the value of management, organisation, training etc.

(iii) MNCs can conceal their true costs of production by the arbitrary valuation of imports and various services provided by the parent company or other subsidiaries.

(iv) They can also conceal the true value of their capital contribution by arbitrary valuation of investments in the form of machinery or know-how.

(v) They often possess greater skills in bargaining than host governments, by virtue of their experience and the calibre of their staff.

167. The government, on the other hand, has two important advantages:

(i) It can nationalise, or threaten to nationalise, foreign investment, paying inadequate compensation to the investors.

(ii) It can renegotiate the terms after the investment has been made, since its bargaining position improves greatly after the MNCs' resources are committed.

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(1) "In some cases, if the country knows precisely what it was buying, there would be no need - or considerably less need - to buy it. Knowledge about knowledge is often the knowledge itself". Streeten, 1973, p.11.

168. The main areas in which bargaining can take place and certain specific items within each area are considered briefly in the following paragraphs.

169. Ownership and Control Many developing countries lay down specific rules on the percentage of equity which can be held by foreign investors, initially and over a period; others do not specify the exact percentage but try to increase the local share by various policies; and others do not interfere with the MNCs at all. Even in cases where the governments have specific rules, exceptions are often made for firms in exceptionally strong bargaining positions which refuse to enter on the terms laid down. We have recommended that local capital should be provided, where possible, in the form of equity rather than loans, and that control should be kept as far as possible in local hands. This must be modified from case to case depending on the value of the investment, the preferences of the MNC concerned, and the effect on the quality of technology transmitted. It can, for instance, happen that a firm may not transfer its latest technology unless it has complete ownership, or at least control, of an investment: or it may not provide as willing and cooperative a technical back-up for the technology transferred.

170. Taxes and Subsidies In most instances tax rates are not varied from one investment to another, so that taxes do not really function as a bargaining counter. Subsidies and concessions may or may not be used for bargaining, depending on their specificity. Many countries grant 'pioneer status' or similar incentives to investments in particular industries or areas, and most grant export subsidies and duty drawbacks on components used to produce exports. These concessions are usually given on a general basis to any firm which qualifies for them; there is, however, no reason why they cannot be varied in particular cases to bargain with investors. We have argued against tax concessions to attract foreign capital in general except for export firms; there may, however, be particular cases where concessions are in order to obtain especially valuable know-how.

171. Protection The extent of effective protection is an important determinant of the desirability of an investment to the host country as well as of its profitability to the investor, yet many governments leave it out of explicit account, both in deciding on which investments are to be allowed and in bargaining. For reasons given above, MNCs are in a particularly strong position to benefit from blanket protection given by automatic prohibition of imports, and it is vital that special attention be paid to this item in striking the final bargain. Furthermore, because conditions change continuously, it is equally vital to renegotiate this element from time to time. The crucial factor in determining protection is, of course, the rate of profit which is to be allowed on the foreign investment, after taking into account risk and the costs of production. It should be the government's intention to pay the lowest rate which would induce the firm in question (or one of a set of firms) to invest; however, in order to determine the real rate of profit being earned, it must depend not on declared profits but check clandestine outflows by means of inflated transfer prices and other payments. It must also, on the other hand, allow the firm to adjust its capital base to take account of inflation, so that rates of profit are not unduly overstated.

172. Composition of output If an MNC is not to be allowed to reproduce the entire range of its operations for developed countries in a less developed one, the range of goods to be produced (including changes in models) must be negotiated at the start and appropriately adjusted over time.

173. Technology We have already indicated the sorts of considerations which should apply to the purchase of technology. Given that the technology is considered appropriate (for the time being at least), the problems which arise for bargaining concern the speed of its diffusion, the restrictive or other conditions attached to its use, the period of the contract (if there is a formal agreement), the use or non-use of patents(1), the provision of back-up services by the parent company, and, most important, the prices to be paid. Royalty rates are presently fixed more on the basis of convention than on any rational economic calculation, and can vary substantially for the same technology between different firms in a country, or between different countries for the same MNC.

174. The scope for official action is vast. In Colombia, for instance, royalty payments were reduced by about 40% by instituting a surveillance and negotiation process, which weeded out payments for outdated technology, pruned down excessive rates, and reduced the life of contracts; the government was also able to remove various restrictive clauses from technological contracts. The Indian Government has also participated actively in the negotiation of technological agreements, and has imposed ceiling on the rates which can be charged for particular types of technology. Due perhaps to the larger percentage of local ownership in India, which has naturally led foreign firms to be tougher in their bargaining over technology sales, the Government has not been able to eliminate restrictive clauses.(2) It has introduced a distinction between 'permissible' and other sorts of export restrictions, the former applying to exports to countries where the foreign firm already supplies the marker. This may be seen as a concession to the superior bargaining position of MNCs, and it reveals a not unwelcome flexibility on the Government's part.

175. Exports Export restrictive clauses are only part of the problem of exporting. The amount of output to be exported now features increasingly in the bargaining process between MNCs and developing countries, with export-oriented firms receiving marked preference over others. Many governments are prepared to negotiate almost any terms on other items if the firm commits itself to exporting a major portion of its output, but clearly the willingness of the firm to do so depends on the domestic costs of production and the geographical access of the country to markets abroad. Exports

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(1) We have not gone into the problem of whether the host country should observe international patent laws or not. A case can be made for less-developed countries opting out of this system altogether (Vaitsos, 1971), though there are dangers that this would hinder the flow of technology, if not its production. Most of the present abuses of the system can, however, be remedied by stricter checks, compulsory licensing, and, perhaps, the renunciation of the system in particular industries such as pharmaceuticles (See Lall, 1974, Scherer, 1971, Penrose, 1973).

(2) See Indian Investment Centre, 1971.

can probably be better promoted over the long run by implementing policies to improve the cost structure than by subsidising them in uncompetitive conditions, but in terms of bargaining strategy countries with large and profitable domestic markets like India may induce MNCs to export even at a loss if they were permitted to make it up by profits on domestic sales.

176. Transfer Pricing This is coming to be recognised as one of the major problems in dealing with MNCs, and one which particularly affects developing countries which have relatively high tax rates or may be unsafe, for other reasons, to declare high profits in.(1) Some countries may not appear liable to a heavy cost on this account simply because their import dependence is relatively low, but even there the cost (in foreign exchange) as a proportion of declared profits may be high, and other methods of moving funds, such as interest, management fees or commissions, may be used to supplement the use of transfer pricing of imports. Unless all these channels are monitored, it would clearly be pointless to bargain on profit rates and protection.(2)

177. There are several ways to deal with the transfer-pricing problem, none of which is completely satisfactory: first, the fixing of tax and tariff rates (on intermediate imports) in such a way that the same revenue is realised whether the firm transmits profits by declaring them or by over-pricing imports; this limits the flexibility of tariff policy and may adversely affect industries which do not have MNCs or firms which would not use transfer pricing.

178. Second, the channelling of all importa through an official agency which negotiates import prices on its own. This may involve delays, heavy administrative expenditures and inefficiency.

179. Third, the taxation, of MNCs on the basis of the profits on their world-wide operations, allocated to particular countries by using a formula based on sales, capital, or some such item. This is, of course, a convenient method of taxation, provided that world-wide profit figures were available; unless every government agreed on the allocation formula, however, it may result in the MNC being over-taxed or under-taxed.

180. Fourth, the checking of transfer prices directly. This would be a cumbersome and difficult task, especially for commodities which do not have open market prices for comparison, and which have high overhead expenses. The U.S. administration's experience of this problem is not very encouraging; however, the amount of savings achieved in Colombia lead one to believe that the efforts may be worthwhile. It may also be possible to engage foreign consultants to handle the

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(1) See Lall, 1973.

(2) Besides the arbitrary pricing of exports and imports to related firms, MNCs may transfer funds via royalties, technical fees, commissions, interest on intra-firm loans, payments for brand-names or trade-marks, and similar service charges. They may also speculate against weak currencies by leading or lagging intra-firm payments. See Robbins and Stobaugh, 1973.

problem, as Tanzania has done, apparently with very satisfactory results,(1) so saving the government from overtaxing its administrative resources.

181. Fifth, the joint taxation of MNCs by all governments which play host to them. While in many ways this could be the ideal solution, it seems for political reasons highly unlikely in practice to be achieved in the forreseeable future.

182. Sixth, the institution of internal checks on MNCs by promoting local shareholding and management. This suffers from the problems that local managers may not be competent to deal with a sophisticated use of transfer prices (or even be aware of it), and that local entrepreneurs can easily be pursuaded to collude with the foreigner in return for payment in foriegn exchange.

183. Perhaps the best solution would be a combination of different policies, especially the third and fourth ones: the allocation of profits using global figures for particular MNCs whose transfer prices were difficult to chaeck, and the checking of prices on the most important commodities which can be assigned arm's length prices. The former would effectively leave the MNC free to set its own prices as long as it paid the host country an agreed percentage of tax on its total profits: in terms of bargaining, therefore, this would probably be the easiest to agree upon.

184. A number of other items, such as the amount of training, the local content of inputs, employment of nationals, arbitration, etc., are also subject to bargaining, but we need not go into them in any detail here.

185. The nature of bargaining involves a large element of flexibility and skill on both sides.(2) The number of factors with which the game can be played is very large, and the information required is also diverse and diffuse. It is not bargaining if the government simply lays down statutory provisions for all these items: it does not get as much as it could from some MNCs while others may be deterred from investing altogether. A number of measures may improve the host government's position.

(i) Centralisation - Often the different items of the bargain are decided upon by different ministries or departments, which do not see the problem as a whole and can act in contradictory ways. The MNC, on the other hand, always acts as a unit and has a clear idea of its objectives (which are of course much narrower and easier to grasp than the objectives of social policy). Unless the government can centralise its bargaining and regulation function, and coordinate all the elements of its bargaining position, it will suffer from a dissipation of its bargaining strength.

(ii) Information - The government needs a vast amount of information to bargain effectively, which it can get partly by research, partly by building up its own store of experience, partly by assistance from sililar countries and partly by help from international

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(1) Neerso, P, 1972.

(2) On the importance of flexibility and coordination, see the Canadian Government's study of 1972.

organisations. The proposed United Nations Commission on Multinational Corporations could prove of great importance in this context because it could coordinate the knowledge of all developing countries as well as drawing upon the expertise of consultants, businessmen, officials and scientists in the developed world.

(iii) Skill - In order to cope with a highly sophisticated and skilled opponent, the host government must devote to the task of bargaining an equally well-trained, informed and honest body of nationals, drawn from the administration, public sector industries, universities and perhaps private enterprise. While less important items on the agenda can be decided at lower levels, and minor problems be settled by reference to standard procedures and rules, the overall package and its more important elements must be reviewed and negotiated by a competent authority which can understand national priorities and implement them without either dogmatism or compromise. There may, however, be a trade off between the need to build up an experienced and mature organisation and the danger of corruption, arising from continuous exposure to powerful temptation from MNCs. These points will be raised again in the last section, but they impinge upon the effectiveness of all the policy measures considered in this paper.

Regulation

Many of the considerations arising in bargaining recur in the regulation of existing investments. The purpose of regulation is, first, to ensure that the laws and provisions relating to foreign investments are met, second, to ensure that the particular bargain struck with an MNC is kept in practice, and, third, to ensure that the renegotiation of the initial bargain is kept up-to-date.

187. Many problems of the regulation of foreign investments apply to industry generally - health and safety measures, anti-monopoly rules, social security, employment and wage provisions, quality control, compliance with various municiple laws, and so on - but some are specific to the former. The main ones are the regulation of remittances abroad (which goes together with taxation), employment of nationals, open or hidden participation in local political activity, and the use of unfair or disallowed (as part of the bargain) business practices. All these have been discussed at some stage already, and we need not go into them again here; what we need to stress here is the importance of efficient regulatory mechanisms which would be able to carry out these tasks, the full reporting of MNC activities, the registration of all forms of contracts and agreements, and a recourse to speedy and fair arbitration in cases of dispute.

CHAPTER VI PROBLEMS IN FORMULATING AND IMPLEMENTING POLICY

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188. We have, throughout this paper, laid enormous stress on the role of the government, in finding out what is conducive to social welfare, in specifying policies which would promote it, and in implementing those policies with honesty and efficiency. At no stage have we tried to make it sound easy;