

Chapter 3

Legal, Technological and Political Environments

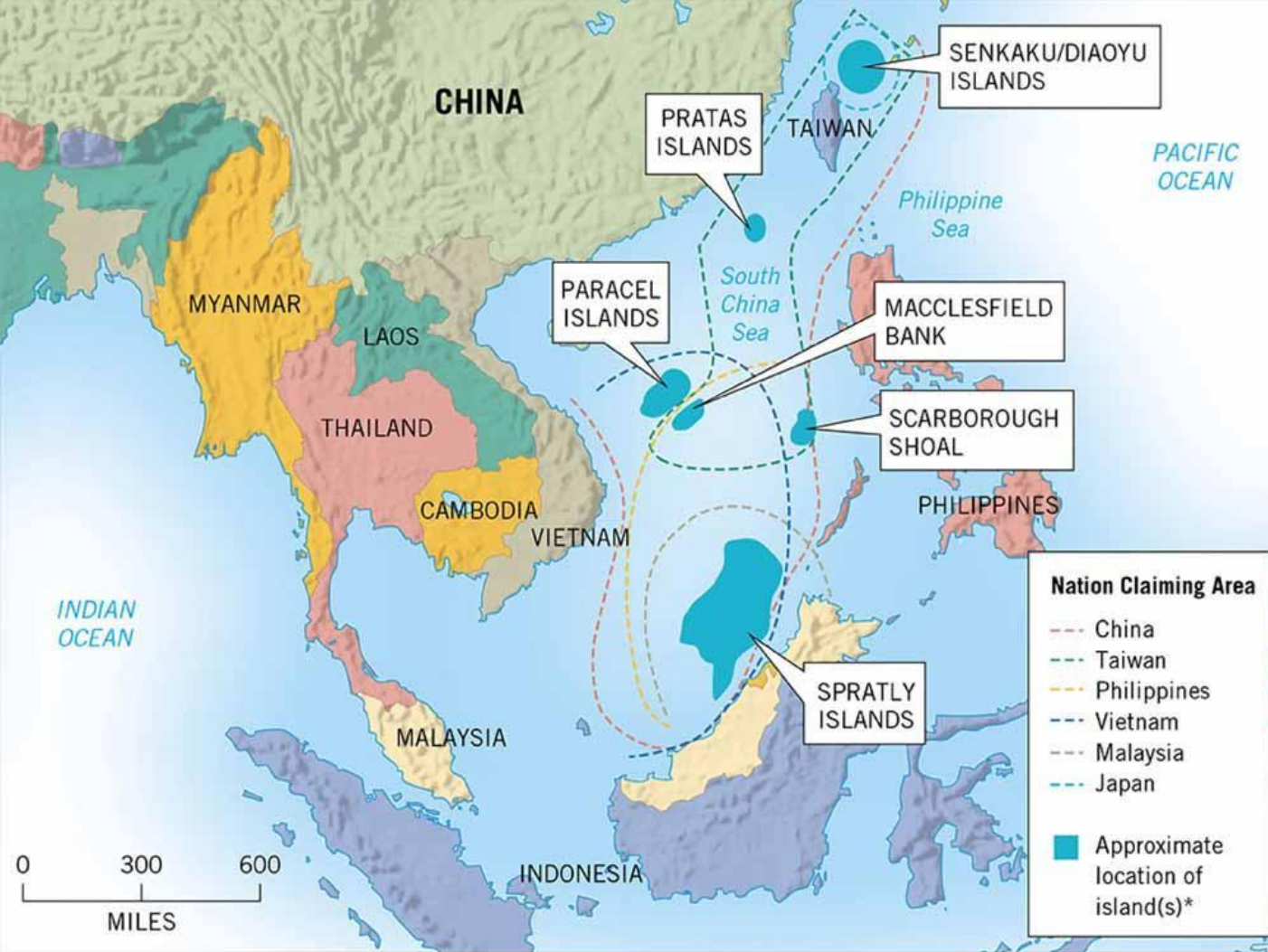
Learning objectives

At the end of this lesson, you should be able to:

3.1 Describe the major types of legal systems confronting international businesses.

3.2 Describe the impact of the host country's technological environment on international business

3.3 Explain how firms can protect themselves from political risk.



South China sea - stretch from Straits of Taiwan and Straits of malacca in south.

Yield 1/10th world's commercial fish catch

Squabbling over 3 small island chains
Spratly islands
Paracel Islands
Pinnacle Islands
Submerged shoals and reefs

Dispute nations

Introduction

Need to understand various dimensions of country's environment on management of firm's international business

why?

Because ALL decisions faced by international managers - who we can hire, any policy or law? Where to build factory? Local government regulations? Zoning restrictions?

LEGAL = law and regulation

TECHNOLOGICAL = available resources, and know how in the country

POLITICAL - existence of government and its continued stability, the activities associated with the governance of a country

The Legal Environment

Domestic firms - must abide laws and customs of home country

International firms - more complex - law of home and host country - can critically affect intl firm conducts business

Some issues

- laws determine markets that it can serve, how much it can charge(price), cost of inputs such as labor, raw materials, technology - wages, source of raw mat.
- Location of activities - high tech products = weak IP protection ?

The Legal Environment: Differences in Legal Systems (1 of 2)

- National legal systems vary dramatically for historical, cultural, political, and religious reasons.
- Rule of law
- Role of lawyers
- Burden of proof
- Right to judicial review
- Laws



Brink's ran afoul of Belgium's labor laws

Example - Labor law
regarding lay off workers

The Legal Environment: Differences in Legal Systems (2 of 2)

● Common Law

- Civil Law
- Religious Law
- Bureaucratic Law
- foundation of the legal systems in the United Kingdom and its former colonies, including the United States, Canada, Australia, India, New Zealand, Hong Kong, Barbados, Saint Kitts and Nevis, and Malaysia.
- Common law is based on the cumulative wisdom of judges' decisions on individual cases through history. These cases create legal precedents, which other judges use to decide similar cases

The Legal Environment: Differences in Legal Systems (2 of 2)

- Common Law
- **Civil Law**
- Religious Law
- Bureaucratic Law
- based on a codification, or detailed listing, of what is and is not permissible
- originated in biblical times with the Romans, who spread it throughout the Western world
- dominance was reinforced by the imposition of the civil law-based Napoleonic Code on territories conquered by French emperor Napoleon Bonaparte during the early nineteenth century

The Legal Environment: Differences in Legal Systems (2 of 2)

- Common Law
- Civil Law
- **Religious Law**
 - based on the officially established rules governing the faith and practice of a particular religion
 - religious rules applied to civil and criminal conduct - theocracy
 - Iran, a group of mullahs, or holy men, determine legality or illegality through their interpretation of the Koran, the holy book of Islam.
- Bureaucratic Law

The Legal Environment: Differences in Legal Systems (2 of 2)

- Common Law
- Civil Law
- Religious Law
- **Bureaucratic Law**
 - Communist countries and in dictatorships is often described as **bureaucratic law**
 - Bureaucratic law is whatever the country's bureaucrats say it is, regardless of the formal law of the land. Contracts can be made or broken at the whim of those in power.
 - Lack of consistency, predictability, and appeal procedures

The Legal Environment: Domestically Oriented Laws

● Impact

- Firm's domestic operations
 - International competitiveness of domestic firms (costs increase - reduce price competitiveness - German high salary govt mandated benefits scheme)
 - Business practices of foreign firms operating outside the country's borders - comply to hygiene standards
- managing its workforce (recruitment, compensation, and labor relations laws); financing its operations (securities, banking, and credit laws); marketing its products (advertising, distribution, and consumer protection laws); and developing and using technology (patent, copyright, and trademark laws).

The Legal Environment: Laws Directly Affecting International Business Transactions

Laws designed to regulate foreign companies business activities

- **Sanctions**

- Embargos
- Export control of dual-use products
- Extraterritoriality
- restricting access to high-technology goods, withdrawing preferential tariff treatment, boycotting the country's goods, and denying new loans

The Legal Environment: Laws Directly Affecting International Business Transactions

Laws designed to regulate foreign companies business activities

- Sanctions
- **Embargos**
- Export control of dual-use products
- Extraterritoriality
- a comprehensive sanction against all commerce with a given country—may be imposed by countries acting in unison or alone

The Legal Environment: Laws Directly Affecting International Business Transactions

Laws designed to regulate foreign companies business activities

- Sanctions
- Embargos
- **Export control of dual-use products**
- Extraterritoriality
- Many technologically advanced countries limit the export of so-called **dual-use products** that may be used for both civilian and military purposes.

The Legal Environment: Laws Directly Affecting International Business Transactions

Laws designed to regulate foreign companies business activities

- Sanctions
- Embargos
- Export control of dual-use products
- **Extraterritoriality**
 - regulate business activities that are conducted outside their borders, a practice known as **extraterritoriality**
 - firms are vulnerable to U.S. antitrust lawsuits if they engage in activities outside the United States that diminish competition in the U.S. market.

The Legal Environment: Laws Directed against Foreign Firms

- transfer ownership of resources from the private to the public sector, **nationalization**
- host government compensates the private owners for their losses, the transfer is called **expropriation**
- host government offers no compensation, the transfer is called **confiscation**
- conversion of state-owned property to privately owned property is called **privatization**
- imposing restrictions on their ability to **repatriate** (return to their home countries) the profits earned

The Legal Environment: Impacts of MNCs on Host Countries

- Impact

- Economic
- Political
- Cultural

The entry of Western retailers like Carrefour into the Chinese market has increased the selection and quality of goods available to the country's consumers. But competition from foreign MNCs makes it harder for mom-and-pop vendors in China's open-air markets to stay in business.



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The Legal Environment: Dispute Resolution in International Business

- **4 Questions**

- Which country's law applies?
- In which country should the issue be resolved?
- Which technique should be used to resolve the conflict: litigation, arbitration, mediation, or negotiation?
- How will the settlement be enforced?

International business contracts - specify answers to questions to reduce uncertainty and expense in resolving disputes

- If a contract does not contain answers to the first two questions, each party to the transaction may seek to have the case heard in the court system most favorable to its own interests, a process known as **forum shopping**.
- Arbitration is the process by which both parties to a conflict agree to submit their cases to a private individual or body whose decision they will honor.
- Whether a foreign court order is enforced is determined by the **principle of comity**. The principle of comity provides that a country will honor and enforce within its own territory the judgments and decisions of foreign courts, with certain limitations.
- The U.S. Foreign Sovereign Immunities Act of 1976 provides that the actions of foreign governments against U.S. firms are generally beyond the jurisdiction of U.S. courts

The Technological Environment

- Foundation of country's technological environment - resources - fertile agricultural land, rich natural resources (oil, gold, diamond), abundant labor resources, - exporters of resources or net importer of resources
- How to change or shape technology environment?
- Investments in infrastructure and human capital
- Technology transfer
- Determinant of technology and willingness to Transfer Technology - Protection of intellectual property rights

The Technological Environment Protection of IPRs (1 of 3)

- International Convention for the Protection of Industrial Property Rights (Paris Convention),
- Berne Convention for the Protection of Literary and Artistic Works,
- Universal Copyright Convention,
- Trade-Related Intellectual Property Rights agreement.

The Technological Environment Protection of IPRs (2 of 3)

Table 3.1 15 Largest Software Markets

	2017 Total Market (in billions)	2017 Pirated Sales (in billions)	2017 Piracy Rate (%)
United States	\$57.4	\$8.6	15
China	\$10.4	\$6.8	66
Germany	\$7.8	\$1.6	20
United Kingdom	\$6.8	\$1.4	21
France	\$6.2	\$2.0	32
Japan	\$6.1	\$1.0	16
India	\$4.4	\$2.5	56
Canada	\$3.7	\$0.8	22

The Technological Environment Protection of IPRs (3 of 3)

Table 3.1 [Continued]

	2017 Total Market (in billions)	2017 Pirated Sales (in billions)	2017 Piracy Rate (%)
Brazil	\$3.6	\$1.7	46
Australia	\$3.0	\$0.5	18
Italy	\$3.0	\$1.3	43
Russia	\$2.1	\$1.3	62
Spain	\$2.0	\$0.9	42
Netherlands	\$2.0	\$0.4	22
Switzerland	\$1.9	\$0.4	21

Source: Based on Business Software Alliance, *BSA Global Software Survey*, June 2018 (<http://www.bsa.org>)

Political Environment

- Business decision - need to assess political environment where firm operates
 - Any level of government laws and regulations - affect viability of business
 - Adverse changes in tax laws can destroy firm's profitability
 - Civil wars, assassination, kidnapping of foreign business people , etc - political stability
- Political risks assessment - systematic analysis of political risks in a country
 - Political risks - any changes in political environment that may adversely affect value of a firm's business activities - 3 categories (nx slide)

The Political Environment: Political Risk

(1 of 4)

● Political Risks

- **Ownership Risk** - the property of a firm is threatened through confiscation or expropriation
- **Operating Risk** - ongoing operations of a firm or the safety of its employees are threatened through changes in laws, environmental standards, tax codes, terrorism, armed insurrection, and so forth
- **Transfer Risk** - the government interferes with a firm's ability to shift funds into and out of the country

The Political Environment: Political Risk (2 of 4)

Table 3.2 Examples of Political Risks

Type	Impact on Firms
Expropriation	Loss of future profits
Confiscation	Loss of assets
	Loss of future profits
Campaigns against foreign goods	Loss of sales
	Increased costs of public relations efforts to improve public image
Mandatory labor benefits legislation	Increased operating costs
Kidnappings, terrorist threats, and other forms of violence	Disrupted production
	Increased security costs
	Increased managerial costs
	Lower productivity

The Political Environment: Political Risk (2 of 4)

Table 3.2 Examples of Political Risks

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The Political Environment: Political Risk Insurance

- To reduce the risk of foreign operations, most developed countries have created government owned or government-sponsored organizations to insure firms against political risks
- Overseas Private Investment Corporation (OPIC) - US Govt
- The Multilateral Investment Guarantee Agency (MIGA) - subsidiary of World Bank
- Private insurance firms, such as Lloyd's of London

Summary

1. Legal systems vary dramatically between countries
2. Laws adopted by governments can influence Global Marketplace in many ways - can impose restrictions on ability to do business or indirectly affect competitiveness by increasing costs or putting barriers/restrictions
3. MNCs hosting in one country can influence economic, political and cultural environments
4. Resolution of international disputes important dimension of legal environment
5. Technological environment important facet of national business environment - how attractive physical resources, labor supplies, IP willingness to enforce rights
6. IB subjected to political risks - continuously monitor political situations embassy, local staffs, and risk assessments

Review Questions

- Describe the four different types of legal systems with which international businesses must deal.
- What is extraterritoriality?
- How can an MNC affect its host country?
- How do expropriation and confiscation differ?
- Under what circumstances do governments try to limit repatriation of profits overseas?
- How do restrictions on repatriation of profits affect MNCs?
- Why do firms engage in technology transfer?
- What is political risk?
- What forms can political risk take?
- What is OPIC's role in promoting international business activity?