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GLOBALIZATION 3.0

How to survive and thrive in a new era of trade, tax and political uncertainty

A BAKER MCKENZIE REPORT

January 2018

Foreword

Despite Brexit and the rise of President Trump's "America First," the global economy is doing remarkably well. China's GDP growth is clipping along at 6%, and while the UK economy is a little weaker, the Eurozone is seeing a rise in household spending and business investment. Key measures of world trade, such as container shipping and air freight, are growing at their fastest rates since before the global economic crisis.

However, there is a darker side. Although globalization has strengthened the world economy as a whole, two-thirds of all households in 25 advanced economy countries saw their incomes stagnate or decline between 2005 and 2014.

It's statistics like this that have created openings for politicians to exploit economic resentment and instate more protective polices. This in turn has created a new phase of globalization, one characterized by the push to innovate, digitize and interconnect like never before counteracted by the fierce compulsion to retract, retreat and return to simpler times.

Both personally and as the chair of a global international law firm, I believe that globalization is a force for good. I don't think a retreat into protectionism is the answer, although I agree we need to make a concerted effort to find a more sustainable model for growing the global economy.

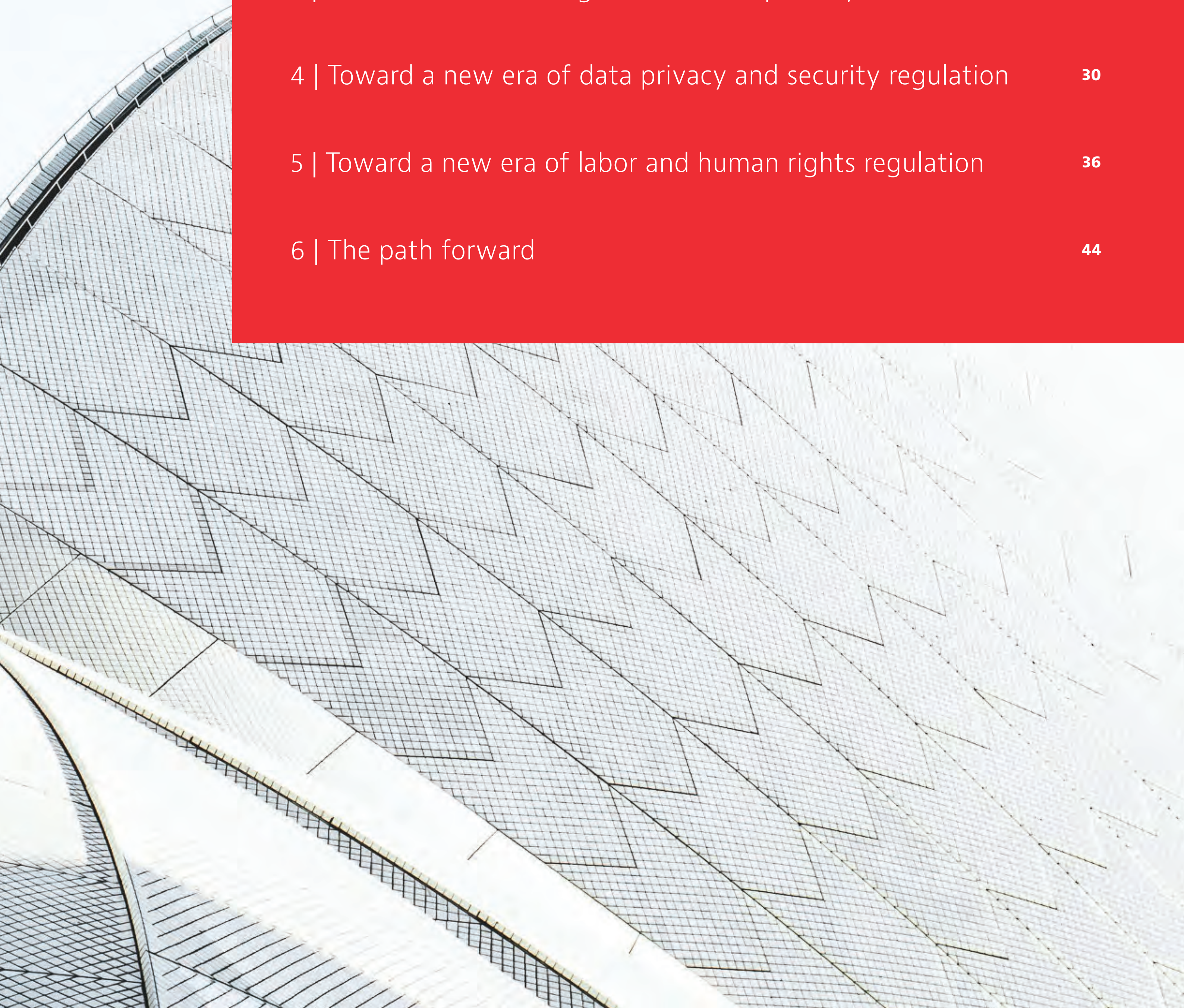
In the meantime we must help our clients contend with the new forces at play, which is what this report aims to do, focusing on four key areas: policies related to trade and investment, tax transparency, data privacy and security, and labor and human rights.

We do our best to answer the questions clients ask us most: How is this new policy, regulation or tax requirement going to affect me? How do we navigate these global opportunities and manage the associated risks?

In this new era of globalization, anything can happen. Our hope is this report makes you better prepared.

PAUL RAWLINSON
Global Chair, Baker McKenzie

Contents



Executive Summary

Multinationals are facing a new era of globalization characterized by the polarized forces of cooperation and competition — a duality that makes for a messy business landscape. On the one hand, the global economic system is becoming increasingly integrated through trade and investment flows and digitization. On the other hand, the global political system is becoming more fragmented amid a backlash against the downside of globalization.

In this report we look at how these forces are shaping policies in four key areas — trade and investment, tax, data privacy and security, and labor and human rights — and identify how companies can prepare for the next era of globalization. Here are the highlights:

International trade and investment gets harder: The trade and investment policy landscape is becoming more complex as nations respond to the effects of globalization, cybersecurity threats, state development strategies and geopolitical risks. The status of various trade agreements is shifting rapidly, and governments are using non-tariff measures like technology transfer obligations, standards requirements, and foreign investment review rules to protect their industries and workers.

As a result, companies need to reevaluate their business strategies, including investment decisions, supply partnerships, and preferential duty access. In addition, as governments in key economies like Germany, the US and Australia place greater scrutiny on foreign investment, it will be imperative for acquirers to develop regulatory strategies early in the deal process to minimize delays, last-minute changes to the deal structure, and even failed transactions.

Managing tax risk becomes trickier: Changing business models, the rise of the digital economy, BEPS implementation, and national tax reform are just a few of the forces dramatically reshaping the global tax system. Even though countries like the US have enacted tax reform, they will need to implement it in ways to encourage investment while at the same time addressing perceived base erosion. This will likely mean that countries will continue to tweak their tax legislation, creating more tax uncertainty. Cross-border cooperation among tax authorities is also making it more difficult for companies to manage tax and reputational risk.

To adapt, companies need to revisit their structure and operations, including existing supply chains, IP ownership models, transfer pricing method selection, permanent establishment exposure, as well as the tax function itself. While regional tax managers have typically overseen local audit activity, a global view is imperative.

Data privacy moves up the compliance agenda: Nearly every company in the world is struggling to manage the broad range of legal and operational risks associated with data. Heightened regulatory scrutiny and more protectionist measures, such as the EU's General Data Protection Regulation that takes effect in May 2018, are making this even more challenging.

To get ready for what lies ahead, companies need to ensure they have an internal governance structure that fosters a culture of data privacy from the top down. This requires having adequate program controls to address key areas such as personal data inventories / records of processing activities, tailored privacy policies and notices, data breach handling procedures, and security and retention policies.

Transparency requirements put the spotlight on labor and human rights: The rapid development of business and human rights standards that companies must uphold under the UN Guiding Principles shows no signs of slowing. Passing laws that require companies to be transparent about their practices related to human rights and gender pay is the latest tool legislators are using to place social expectations on corporations.

To minimize legal and reputational risk in the area of human rights, corporations must first conduct a risk analysis of their current activities and operations, review or implement human rights policies and supplier codes of conduct based on the assessment, and take swift action to investigate and remedy problem areas.

1

GLOBALIZATION 3.0

Preparing for the next era of globalization

Every summer, dozens of professional cycling teams spend weeks competing in the Grand Tours. Fundamental to each team's race strategy is for the members to ride in close proximity to each other, in what's known as a peloton. The "drafting" effect that's fundamental to the peloton greatly increases the riders' speed and efficiency. But the cooperation gradually evolves into head-to-head competition, as each rider is focused on completing the race with as fast a time as possible. The most lucrative awards are, after all, bestowed on the basis of individual performance.

The peloton is a useful metaphor for today's state of globalization. While nations are cooperating with each other in a number of areas to advance prosperity and security, there are also healthy doses of competition and unilateralism, driven by a desire to realize a variety of "rewards": tax revenue, corporate data, foreign direct investment, and the like. To the untrained eye, it's not always clear why nations have chosen to cooperate or compete in particular areas, nor what may lead them to alter their posture in the future. Yet their choices have profound implications for the global economic outlook and corporate activity.

Global policymakers have raised concerns about protectionism depressing global growth, and projections for total M&A and IPO activity vary significantly depending on whether nations move toward protectionism or take actions to accelerate global trade. For example, our analysis of the impact on global transaction flows of the US taking a more protectionist stance shows that rather than rising in 2018, global M&A levels could fall by up to a trillion dollars and IPO activity by half.

These cross-currents of cooperation and competition pose a challenge for companies of all sizes and in all industries since the policy ramifications can cascade far beyond the intended targets. And this legal and policy uncertainty stands in contrast to what's supposed to be distinctive about today's business climate, where "going global" is easier and more attractive than a few decades ago thanks to lower-cost technology and the growth of the global middle class. While these conditions still exist, they must be squared with new operating risks found at national – and even local – levels.

If the 19th and early 20th century with its UK-led unilateral liberalization represented Globalization 1.0, and the post war era with its US-led international order constituted Globalization 2.0, we may be witnessing the emergence of Globalization 3.0. In this new era, technology and existing trading and investment patterns anchor sustained integration, while national politics pull in the direction of localization.

Drawing on insights from a diverse collection of Baker McKenzie partners, this report:

- explores different dimensions of the cooperation and competition we see at play throughout the world in key areas — trade and investment, tax, data privacy, and labor and human rights

- highlights what we expect will be some of the defining characteristics of the next era of globalization and

- offers strategies for global businesses to navigate a rapidly evolving and more fragmented global marketplace

By providing this outlook, we aim to provide corporate leaders with a greater understanding of key trends so they can anticipate, influence, and better prepare for the changing world order.

How we got here — the uneven state of globalization

There were two seminal political developments in 2016: the UK's vote to exit the European Union and Donald Trump's victory in the US presidential election. While diverse dynamics drove each development, a key factor in both countries appeared to be diminished public support for deeper international integration, reflected in growing hostility to cross-border flows of goods and people.

In a commencement address before both events, then chief executive officer of GE Jeffrey Immelt provided a number of reasons for the brewing disgruntlement throughout much of the world about globalization: "Many people feel left behind. The global economy is growing too slowly. Some workers have been displaced by outsourcing, the middle class has been squeezed and income inequality has risen to unacceptable levels. As technology and globalization race forward, people understandably fear their impact on jobs and incomes, and distrust the motives of companies and government."[1]

These conditions are borne out by a number of indicators showing a toxic cocktail of prolonged wage stagnation, high unemployment, and economic sluggishness that has afflicted much of the world.

- Between 2005 and 2014, about two-thirds of all households in 25 advanced economy countries saw their incomes stagnate or decline.[2]

- In the US, market incomes declined for 81% of households from 2005 to the end of 2013.[3]

- The economic growth rate in emerging markets steadily declined every year from 2010 through 2015. While growth has strengthened in recent years, the World Bank has found that much of the slowdown since 2014 reflects productivity declines growing out of aging populations – a significant long-term challenge for these countries.[4]

These figures have created an opening for politicians to exploit economic resentment, which typically results in policies aimed at curtailing competition. The wide-ranging policies can span from higher tariffs on imported goods to restrictions on the flow of cross-border data and the movement of people. While political posturing often drives policy proposals, many of which have no hope of enactment, they nonetheless contribute to a challenging environment for multinational companies.

Defining characteristics of the next era of globalization

HEIGHTENED TRANSPARENCY

"Transparency has become a defining feature of today's business climate. It's easier than ever to access information about companies, whether it relates to their quarterly revenues or their commitment to social responsibility. While companies can use this transparency to their advantage – disclosure can help to demystify their activities – companies are also vulnerable to the disclosure (and global dissemination) of unauthorized information." —MATTIAS HEDWALL

"Transparency legislation is increasingly being used as a means to regulate complex problems. We are seeing this in various contexts from supply chain transparency requirements in the US and the UK to gender pay reporting laws." —MONICA KURNATOWSKA

TECHNOLOGICAL DISRUPTION

"The biggest drivers of globalization have been technological, from steamships to containerization to the internet. Technology may cut in a different way in the future. 3D printing and automation, for example, may change supply chain dynamics. Labor arbitrage may be replaced by proximity to customers as a driver." —ROD HUNTER

"Technological advances are creating new categories of jobs and displacing others, creating anxiety for many people. At the same time, public confidence is essential if companies are going to be able to fully leverage new technologies." —GIL ZERRUDO

MORE COORDINATED AND AGGRESSIVE GOVERNMENT ENFORCEMENT

"There's been a huge increase in countries cooperating on tax enforcement. While the cooperation has been going on for some time, it used to be limited to small groups. Now we're seeing multi-jurisdictional audits across jurisdictions." —MARY BENNETT

"Government agencies in the US and elsewhere have become much more sophisticated in their investigations and enforcement, coordinating across multiple subjects and agencies. For example, an investigation into immigration violations will sweep up labor conditions and wage issues and multiply across states." —BETSY MORGAN

INCREASING NEED FOR NEW MANAGEMENT SKILLS AND ORGANIZATIONAL APPROACHES

"For many of our clients, new staffing models such as employee sharing and crowd employment are part of a drive to attract talent, not cut costs. Companies are going to need a strong internal HR compliance function in place to work with what is going to be a very different workforce that presents different risks and opportunities." —SUSAN EANDI

"It's no longer sufficient to have regional tax managers oversee local audit activity. With tax authorities sharing information with their counterparts in other countries, companies need to have their tax functions overseen by global tax managers." —KIRSTEN MALM

"The heightened transparency around company activities, particularly via social media, makes human resources work more challenging. Corporate missteps – often by employees far from headquarters – can quickly be portrayed as violations of human rights and become global issues requiring C-suite attention. And that means companies need a completely new skill set in leadership. But today, company managers still tend to be very local. That needs to change." —GUENTHER HECKELMANN

SOURCING AND MOVING TALENT BECOMES MORE CHALLENGING

"Each country is walking a fine line between being protectionist of its workforce and trying to incentivize investment. Right now, there's a lot of fear about the movement of people and how it will be perceived in the destination country." —BETSY MORGAN

PRIVACY MOVES UP THE COMPLIANCE AGENDA

"The greater focus on accountability means that there will be more pressure to have board room attention and strong privacy governance. Many companies also will have a specific legal obligation to appoint a data protection officer." —BRIAN HENGESBAUGH

"Data privacy is becoming more important to employees as they increasingly take action to protect their privacy rights. The concept of privacy by design will be fundamental to managing regulatory compliance risk and maintaining the trust of the workforce." —JULIA WILSON

STAKEHOLDER ENGAGEMENT BECOMES MORE CRITICAL

"Rather than ignoring labor and human rights issues until they become a crisis, companies that engage with key stakeholders can gain valuable commercial intelligence and build goodwill." —KEVIN COON

"In this environment, with so many changes to tax policy being contemplated, it's more important than ever for companies to engage with governments." —JOSHUA ODINTZ

POLITICAL CLIMATE POSES NEW CHALLENGES TO BRAND AND CULTURE

"An early impact of the rising tide of nationalism is that multinational companies can find themselves under pressure to take a position and make a statement about what they stand for. How to balance global and local values and politics can be a fraught issue." —MONICA KURNATOWSKA

"Organisations can tie themselves in knots trying to achieve a 'one size fits all' approach to workplace policy and communication. Organisations tend to find their task easier when they apply 'the voice' of their brand but flex content to their local workforce audience." — JULIA WILSON

GOVERNMENTS SEARCHING FOR NEW SOURCES OF REVENUE

"More governments are targeting misclassification of employees to enhance tax and social security revenues, as well as enforce wage and hour laws. At the same time, companies often significantly underestimate the financial risk exposure to these types of claims." —WILLIAM DUGAN

"Companies in the US and Europe are facing more challenging audits all around the world on their transfer pricing and entitlement to treaty benefits on cross-border investments. They are having more withholding taxes imposed on their flows of income." —MARY BENNETT

RISING INFLUENCE OF NON-GOVERNMENTAL ACTORS

"There's been a polarization of the tax policy debate, particularly as non-governmental organizations have begun to play a bigger role than in the past, and with European companies being pretty much absent from the debate." —WOUTER PAARDEKOOPER

"Union leaders participate in meetings of the G7 and the G20. They recognized that their model needed to change and they have found other ways to achieve influence." —KEVIN COON

COMPANIES CONSIDER LOCALIZATION TO MANAGE RISKS

"Some large companies are beginning to double down on the concept of being local, more than global, so that they don't get in the middle of a policy discussion between the US and the rest of the world. They want to be seen as strong, local contributors to wherever they may be doing business." —MIGUEL NOYOLA

"There's evidence that more people are placing a higher value on locally sourced and produced goods and services. Some companies are considering shifting their supply chain to become more local not only to manage uncertainty and control production, but also to respond to changing consumer values." —MANUEL PADRON

2

Toward a new era of

TRADE AND INVESTMENT POLICY

While the previous generation of trade liberalization has been extraordinary, particularly in developed markets, many governments are recalibrating their approach to trade and investment in response to the effects of globalization, technological advances, state development strategies and geopolitical risks.

This dramatic rebalancing has the potential to slow economic growth, as multinational companies work out whether to forge ahead with their deal making or put investment decisions on hold. They also have to consider how to raise capital and allocate resources for trade deals and cross-border transactions when it's unclear how the rules and terms of trade and foreign investment are going to change. Indeed, according to our recent survey, more than half of business leaders in the Asia-Pacific region cite trade deal uncertainty as one of the key complexities they face today.[5]

"While it's difficult to predict concrete steps – and to separate political rhetoric from policy changes – multinational companies need to recognize that the landscape has changed," says Mattias Hedwall, Global Chair of Baker McKenzie's International Commercial & Trade Practice Group. "Trade liberalization is likely to become more difficult, and cross-border investment is likely to attract more attention from policymakers, advocacy groups, and the media."

COOPERATIVE TRADE AND INVESTMENT FORCES CONTINUE

Amid the changes unfolding across the global economic landscape, it's useful to remember that trade and foreign investment are deeply woven into the fabric of the world economy. Trade represents 58 percent of global GDP and FDI flows have exceeded $1 trillion every year since 2005.[6] And there is evidence of new global cooperation. For example, last year:

- The Trade Facilitation Agreement (TFA) entered into force – the first WTO multilateral deal concluded since its founding in 1995. Full implementation of the TFA is projected to cut members' trade costs by an average of 14.3 per cent and add as much as 2.7 percentage points per year to world trade growth by 2030.[7]

- Japan and the EU finalized a free trade agreement (excluding investor disputes) that covers over a quarter of the global economy.

- The Comprehensive Economic and Trade Agreement (CETA) between the EU and Canada entered into force provisionally, ending 98% of tariffs on goods.

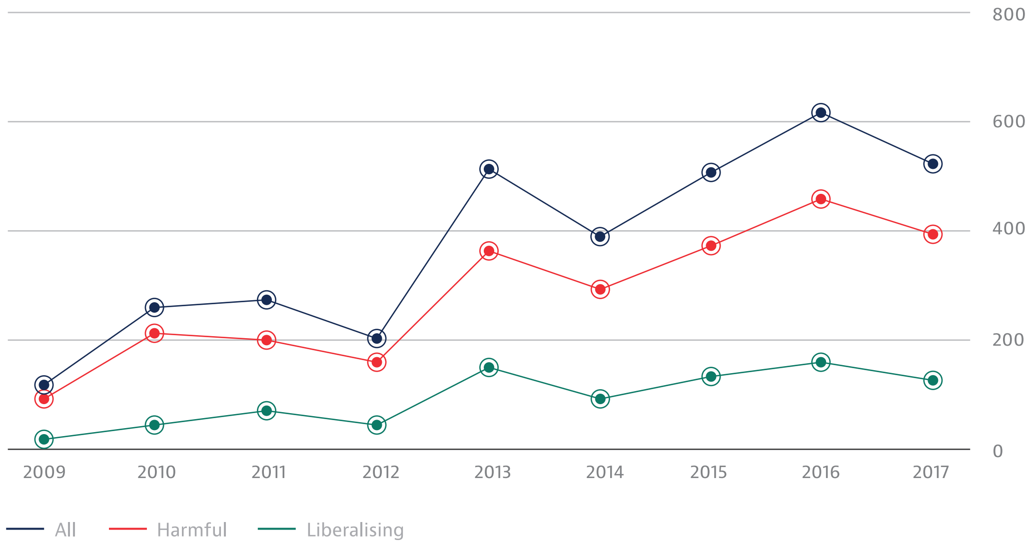
- Eleven signatories of the now defunct Trans-Pacific Partnership (TPP) agreement (excluding the US) announced the outline of the Comprehensive and Progressive Agreement for Trans-Pacific Partnership.

More broadly, from 2012 to 2016 the number of trade liberalization measures enacted by governments around the world nearly tripled (though the absolute numbers were low compared to the volume of protectionist measures).[8] That's a reminder, says Miguel Noyola, an international commercial partner in Washington, DC, that "even in these challenging times, most countries recognize that there are clear benefits from trade."

COOPERATION ON TRADE AND INVESTMENT IS BECOMING MORE DIFFICULT

While countries continue to look to free trade agreements to support closer economic integration, a striking development in the post-financial crisis period has been a surge in restrictive trade policy. Since the height of the crisis in November 2008, governments around the world have implemented more than 2,300 protectionist measures, according to Global Trade Alert.[9]

INTERVENTIONS PER YEAR



Source: Global Trade Alert

The environment for large trade agreements is also becoming more challenging, as evidenced by the negotiations over CETA. While it went into provisional application in September 2017 after ten years of negotiations, to fully enter into force it needs to pass 42 national and regional parliaments in 28 EU countries – no small feat in view of the vocal opposition in many countries and Belgium's challenge to the Investment Court System in front of the European Court of Justice.

"The negotiations between the EU and Canada were extremely hard to conclude even though there were obvious benefits for both parties," says Hedwall. "One regional government in one Member State – the Belgian regional parliament of Wallonia – was able to hold up the agreement for quite some time, and we are likely to see more of this in the future. Different interests at a local level can have a huge impact on the ability to conclude big multilateral agreements."

Even bilateral and regional trade agreements may be under threat. The WTO has advanced a scenario where violations of such agreements become widespread, unilateral changes are introduced, and re-negotiations are forced or even unilaterally revoked.[10] The likelihood of this adverse trade scenario being realized has dramatically increased, particularly as the Trump Administration has made a number of threats to withdraw from existing trade agreements such as NAFTA and KORUS.

"The debate over whether particular trade agreements are 'fair' is intensifying. This is creating much more uncertainty in the trade environment, which in turn is complicating companies' ability to make long term investment decisions," says Manuel Padron, the Latin America Chair of Baker McKenzie's International Commercial & Trade Practice Group.

On the foreign investment side, regulation is becoming more complex as advanced economies respond to record levels of Chinese investment, increased activity by state-owned enterprises and sovereign entities, and changing ideas about national and economic security. As our recent report, *Rising Scrutiny*, highlights, seven of the nine most advanced economies have changed their foreign investment review procedures since 2014 (Australia, Canada, France and Germany) — or are considering doing so (the UK, the US and the EU) — to allow for greater government review of cross-border investments.[11]

Tensions between the US and China have continued to rise in early 2018, with one deal blocked already and debate over reciprocity and technology transfer. "No-one wins a zero sum game and cooperation between the world's largest economies is the only way to continue economic growth," says Danian Zhang, chief representative of Baker McKenzie's Shanghai office.

THE CHANGING GLOBAL TRADE ORDER COULD DRAMATICALLY IMPACT M&A AND IPO ACTIVITY

In our Global Transactions Forecast released with Oxford Economics in late 2017, we forecast an uplift in M&A and IPO activity in 2018 as dealmakers and investors gain greater confidence in the business prospects of acquisition targets and newly listed businesses.[12] Two alternative scenarios, however, demonstrate the wide potential swing based on trade and investment policies.

In the upside forecast, sustained growth in the Chinese economy and stronger near-term growth in the US spur global optimism, accelerated global trade and a higher volume of deal-making in key trading sectors, such as manufactured goods and internationally-traded service sectors.

The second scenario is based on a return to US protectionism and anticipates a far more negative outcome. In this model, the US imposes tariffs of 45% and 35% on Chinese and Mexican merchandise goods, respectively, and also raises tariffs on imports from South Korea and Taiwan, prompting these countries to retaliate with similar tariffs on US exports. In addition, deportation of illegal immigrants and curbs on legal immigrants result in a decline in the size of the US labor force. Under these conditions, M&A activity could fall by up to $1 trillion in 2018 and around $500 billion in 2019.

TRANSACTIONS FORECAST TOTAL M&A ACTIVITY (US$T)

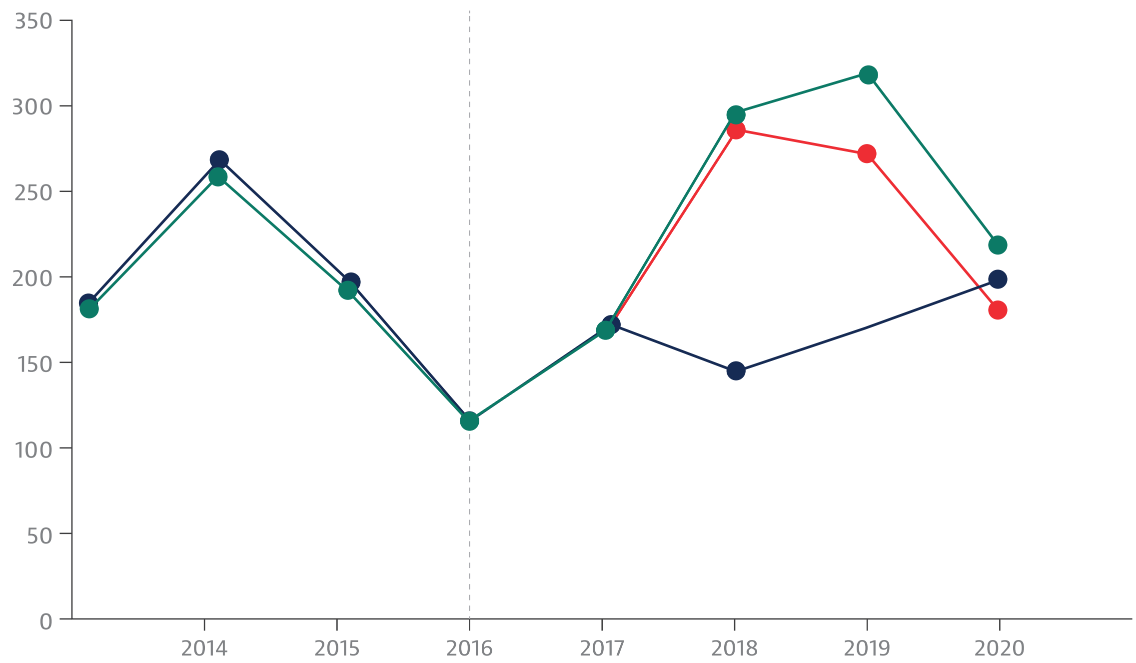
Baseline

Policy missteps by US administration

Cyclical acceleration in global trade

Source: Baker McKenzie and Oxford Economics 2018 Global Transactions Forecast

TRANSACTIONS FORECAST TOTAL IPO ACTIVITY (US$B)



Baseline

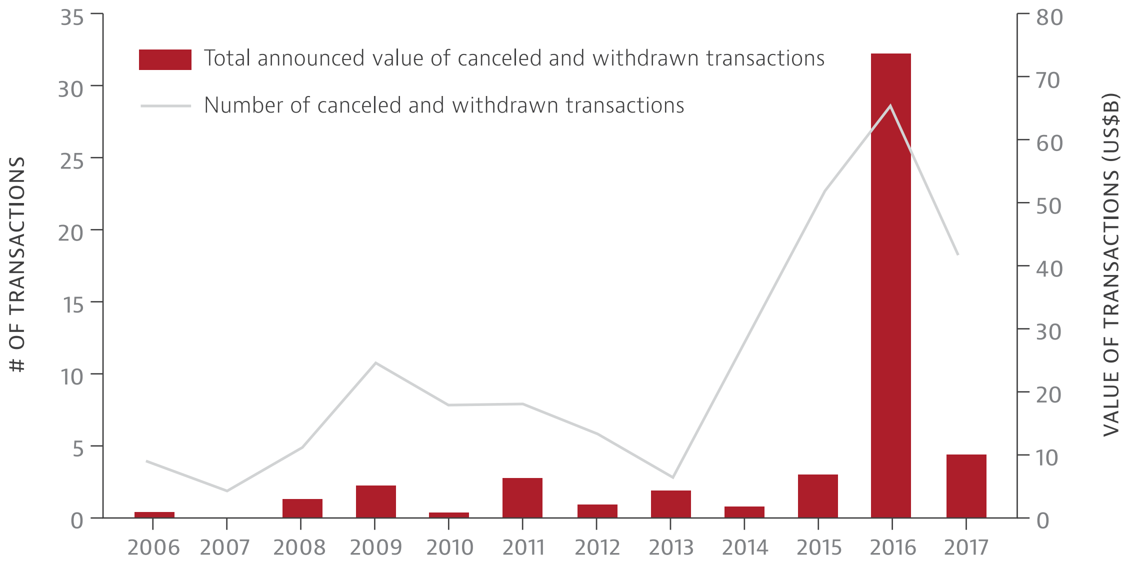
Policy missteps by US administration

Cyclical acceleration in global trade

Source: Baker McKenzie and Oxford Economics 2018 Global Transactions Forecast

Changes to investment policy could also impact deal activity. In 2016, for instance, Chinese investors walked away from 30 deals for US and European companies worth $74 billion where regulatory and political scrutiny was a contributing factor.[13] Similarly, while the total number and value of abandoned deals declined in 2017 — mostly because of Beijing's tougher regulatory stance on outbound investment — overseas regulators and political backlash sunk more Chinese deals than ever before.[14] More than two-thirds of the total withdrawn / canceled transactions last year can be attributed to overseas regulatory intervention, with at least $7 billion in deals terminated because of CFIUS concerns.

CANCELED AND WITHDRAWN CHINESE FDI TRANSACTIONS IN NORTH AMERICA & EUROPE



Source: Rhodium Group. Includes transactions that were publicly announced by the buyer but then withdrawn or canceled. Europe includes the EU-28 and the European Free Trade Association (EFTA) countries: Iceland, Liechtenstein, Norway, and Switzerland. North America includes the United States and Canada.

THE CHALLENGES AHEAD

While global trade has borne the brunt of the backlash against globalization, technological change has been the larger force behind job losses in manufacturing. According to a recent study, 85% of US manufacturing job losses between 2000 and 2010 are actually attributable to technological change – primarily automation – and not international trade.[15]

New technologies from automation and additive manufacturing to AI could dramatically alter trade patterns as companies think differently about their business models and footprints. Similarly, factors other than low wages, such as customer needs, the availability of low-cost transportation, or access to skilled employees, may play a bigger role in investment decisions, reshaping supply chains.

The exponential growth of digital trade – which lacks a global framework – is also creating uncertainty for multinational companies. According to McKinsey, cross-border data flows grew by 45 times between 2005 and 2014, generating $2.8 trillion in economic value in 2014 – a greater impact on world GDP than global trade in goods.[16] Many governments have responded to these changes by seeking to control (and tax) digital trade through measures such as filtering and/or blocking cross-border data flows, implementing data localization requirements, and imposing news aggregation fees.

On the foreign investment front, a looming question is whether, and to what extent, countries choose to consider economic interests in screening investments, either explicitly or within the rubric of national security. While some countries currently evaluate the economic impact of foreign investment as part of the review process – for example, Canada's "net benefit" test – others have focused on sectors traditionally associated with national security. This may be changing, even in the absence of changes to regulations, as governments think more broadly about their national interests.

PREPARING FOR THE EVOLVING TRADE AND INVESTMENT LANDSCAPE

As countries throughout the world adapt their trade and investment policies to respond to new risks, multinational companies will need to closely monitor the landscape. Below we offer strategies to help companies capture the benefits of free trade agreements and get deals through.

Think strategically about trade

In order to harness the benefits of the multilateral agreements that are taking shape, companies should:

- Review FTAs, including duty phase-out schedules, when planning future expansion and distribution activities.

- Consider new suppliers to take advantage of preferential duty programs and rates.

- Consider the use of FTAs for investment structuring purposes, such as to reduce foreign investment limits and to protect investments. Service and investment commitments in FTAs provide qualified investors / service providers with preferential market access. This will impact holding company structures and the activities that must be performed by holding companies to benefit from preferential access.

- Consider rules of origin that make it easier to achieve more flexibility in sourcing operations, but still ensure entitlements to preferences.

- Review pricing and sourcing to ensure benefits are being derived from FTA duty preferences when purchasing goods from a distributor or supplier and that the company can claim preferences when assembling materials from many sources.

Ensure a robust compliance program

As companies develop increasingly sophisticated and optimized global supply chains, it is critical to ensure their programs and controls are sufficiently robust to support compliance with the web of international trade rules. Unsubstantiated or incorrect certifications can result in penalties and retroactive duties with interest. To minimize risks, companies should:

- Conduct an international customs and trade compliance health check on internal systems, processes and controls, tariff classification, valuation and origin.

- Ensure suppliers meet origin rules. Origin audits and investigations are becoming more common, particularly in the Asia-Pacific region, and will continue to proliferate as FTAs increasingly provide for self-certification.

- Obtain warranties and indemnities from suppliers and conduct regular internal audits and visits.

Anticipate e-commerce and privacy provisions

The Comprehensive and Progressive Agreement for Trans-Pacific Partnership leaves intact TPP provisions promoting electronic commerce and eliminating barriers such as “data localization” requirements. These provisions were built on the foundational concept that data must be able to flow back and forth across borders, subject to certain baseline protections. While the future of digital trade rules is uncertain, companies are likely to see more regulation in this area. To prepare, companies should:

- Examine current privacy policies and procedures to ensure that they are broad enough to address consumer data and marketing issues (e.g., online collection of data, opt-in/opt-out requirements for electronic email solicitations) and are not focused only on home country rules and regulations. Companies need to consider each country’s legal and regulatory framework.

- Ensure that their privacy governance structure is flexible enough to address differences across countries, including standards of stricter regions such as the EU. A one-size-fits-all approach may not work across the organization.

- Prepare for heightened focus on privacy and cyber security-related issues by regulatory authorities, as well as privacy advocates and individual consumers.

- Consider non-tariff barriers associated with e-commerce activities.

Conduct an early risk assessment of foreign investment review risks

Foreign investment is a hot-button issue in many advanced economies. While the vast majority of transactions continue to be approved, uncertainty related to foreign investment review risk inevitably makes some buyers less attractive than others. This activity underscores the need for investors to prioritize foreign investment review risks as early as possible, certainly pre-approach, to determine if potential concerns exist. In addition, to increase the likelihood of getting deals approved, foreign investors should:

- *Elevate national security risks for investors with any hint of a state affiliate:* This includes investors that are directly or indirectly government-owned, -controlled, or even -influenced, as well as private investors headquartered in countries with state-directed economies.

- *Take a global view of national security risks:* Early identification of impacted jurisdictions and cooperation between counsel on strategy are paramount. Even minor operations or activities in a country with strong national security laws can potentially present roadblocks, and countries are increasingly likely to coordinate their efforts. “Before engaging in any new project, investors need to assess carefully its commercial viability. As governments tighten regulatory and legal requirements and scrutiny, Chinese investors in particular have to factor in the increasing cost of compliance,” says Bee Chun Boo, a partner in Baker McKenzie’s Beijing office.

- *Craft a public and government relations strategy:* Foreign investment reviews can be highly political and susceptible to negative media attention, and developments on this front in one country can easily impact the perception and process in another. “Apart from the exercise of a legal right, in practice, whether a bid is successful depends on how the government, investors, the press, unions and others talk about it,” says Tim Gee, a Baker McKenzie M&A partner in London. “It’s critical to manage stakeholder interests to get a fair wind behind the offer.”

- *Engage with the reviewing body early:* Foreign investors should work with counsel to engage with relevant officials up front, even on an informal basis without disclosing the client’s name, to identify and quantify risks. “From a purely regulatory standpoint, the earlier you go in, the more receptive the regulators are likely to be because they feel you’re being respectful. At the end, you’re more likely to negotiate a favorable outcome than if you leave things to the last possible minute and take advantage of every statutory right,” says Arlan Gates, a regulatory partner in Baker McKenzie’s Toronto office.

- *Understand the process and timeline:* The process and time frame for screening investments can vary widely and may not be as predictable as statutory provisions suggest. The procedural complexities can be even greater for multi-jurisdictional deals.

"Before engaging in any new project, investors need to assess carefully its commercial viability. As governments tighten regulatory and legal requirements and scrutiny, Chinese investors in particular have to factor in the increasing cost of compliance."

BEE CHUN BOO

Baker McKenzie, Belt and Road: Opportunity and Risk - The prospects and perils of building China's new Silk Road (2017); www.bakermckenzie.com/ChinaBRI

3

Toward a new era of

GLOBAL TAX TRANSPARENCY

Uncertainty about globalization has itself been globalized, with populations throughout the world questioning whether the mostly unfettered flow of goods, services, information, and people is a net positive or a net negative. The discontent in some countries is intimately linked to growing distrust of two pillars of virtually every economy: government and multinational companies. At the nexus of the relationship between government and multinational companies is the public policy that is frequently a source of debate: taxation. There is a sense among many people that globalization benefits large companies and not average citizens, with some asserting that companies are not paying their "fair share" of taxes (even if their tax positions are lawful).

Against this backdrop, one of the most noteworthy global economic policy developments in decades – the OECD's base erosion and profit shifting (BEPS) Project – is dramatically altering the international tax system by encouraging governments to close loopholes, improve transparency and "better align rights to tax with economic activity."[17] While cross-border tax cooperation has always existed, the BEPS Project encompasses more countries and more issues. As a result, multinationals are facing the biggest changes to how and where they're taxed in more than 50 years, according to Baker McKenzie partner Caroline Silberztein.

At the same time, countries are still finding ways to compete as they seek to attract investment and increase tax collections. This activity is creating greater uncertainty for international tax planning strategies and raising the stakes when it comes to compliance. Changing business models, the rise of the digital economy, technological advances such as automation, and national tax reform – particularly in the US – are further complicating the tax policy landscape. Below we highlight the conflicting forces reshaping tax policy and the resulting risks and opportunities for multinationals, which extend well beyond the tax department.

THE CROSS-BORDER COOPERATION RESHAPING TAX POLICY

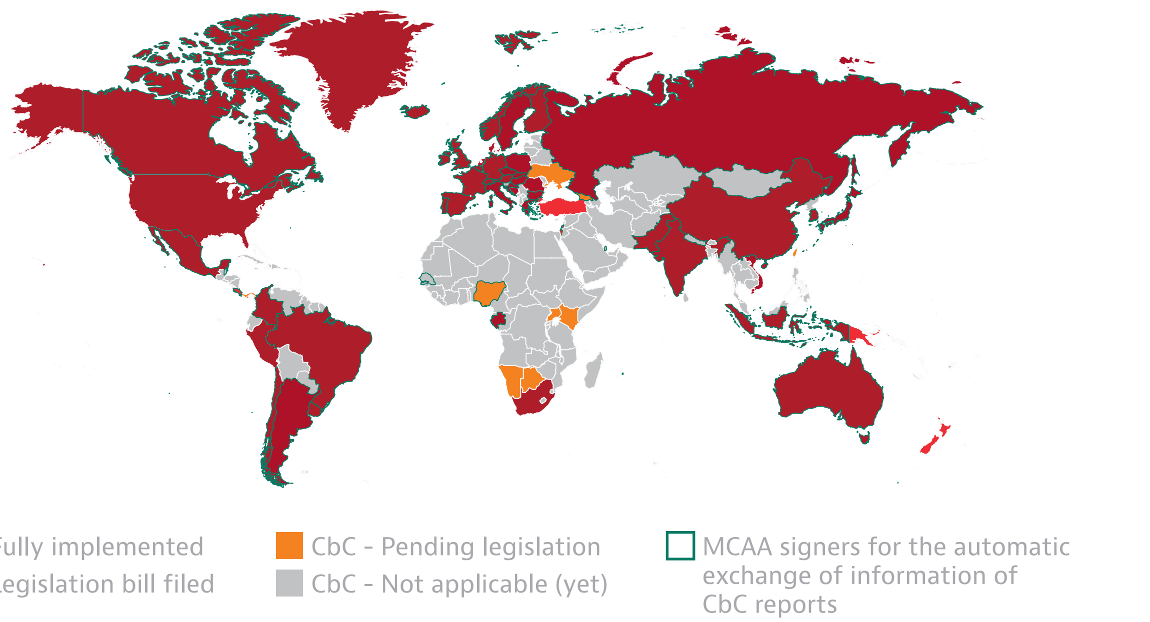
The scope of the OECD/G20 Inclusive Framework on BEPS is unprecedented. It involves more than 100 countries and jurisdictions and includes the implementation of 15 action plans covering various dimensions of the operating landscape for multinational companies from the digital economy to dispute resolution.[18] Nations are moving forward quickly to establish the necessary legal framework to implement the BEPS package of measures with the aim of curtailing corporate tax planning strategies that reduce tax liability by shifting profits to locations where companies have little or no economic activity.

Several of these measures are notable for their focus on transparency and heightened cross-border cooperation. For example, the BEPS Project's Action 13 aims to develop rules for transfer pricing documentation to enhance transparency for tax administrations and provide the information needed to conduct effective transfer pricing risk assessments and audits. Under the three-tier system for documentation, multinational companies must deliver to tax administrations a detailed disclosure of where they record profits and sales, employ staff, hold assets and pay and accrue taxes.

This disclosure – known as "Country-by-Country Reporting" (CbCR) – "represents a break with past tax policy," says Mary Bennett, a Baker McKenzie partner based in Washington, DC and former head of the OECD's tax treaty, transfer pricing and financial transactions division. "It imposes a new obligation on multinationals to generate detailed information on their global operations for the digestion of every country in which they do business around the world. And it's going to involve extensive information sharing among governments."

COUNTRY-BY-COUNTRY REPORTING (CbCR)

CbCR requires detailed disclosures. Over 60 countries or jurisdictions, including many of the world's largest economies, have implemented an obligation for relevant multinational companies to file CbCRs.



Current as Jan. 15, 2018; source: http://www.oecd.org/tax/automatic-exchange/country-specific-information-on-country-by-country-reporting-implementation.htm

Another indicator of the global push for transparency and greater cross-border cooperation among tax authorities is the BEPS framework for the compulsory and spontaneous exchange of information about tax rulings (BEPS Action 5). By mid-2017, exchanges of about 6,000 tax rulings had already taken place between tax administrations around the world, with thousands more underway.[19] The effect of this compulsion is clear – transactions or arrangements that may present BEPS concerns will be reported to tax administrations in other relevant countries.

Together, CbCRs and automatic information exchanges provide immediate transparency about the multinational's operations and tax liabilities globally. Since the CbC reports provide information without an appropriate commercial context, the information may increase the risk of tax disputes. Indeed, there is already evidence that BEPS is spurring audit activity, with companies facing identical audits in multiple countries.

While BEPS is at the center of the push for transparency, political momentum is spurring related tax activity and cooperation across various country blocs. For instance, in July 2017, the BRICS countries – Brazil, Russia, India, China, and South Africa – announced a landmark tax cooperation agreement. And the European Council has resurrected a project to study the imposition of the Common Corporate Consolidated Tax Base in the EU, which essentially would substitute formulary apportionment for the arm's length principle to allocate the tax base for transactions within the EU.

While the success and timing of any specific effort is difficult to predict, the directional trend is clear. Tax policymakers are looking for new tools to respond to a digitized and internationalized economy and a certain level of global cooperation is helpful to advance national aims.

AMID COOPERATION, COMPETITION CONTINUES

At the same time, the cooperative spirit underpinning the BEPS Project and other initiatives has not done away with the cross-border competition that's been fundamental to tax policy for decades. Corporate tax rates remain a fundamental differentiator for countries trying to attract foreign investment (or keep domestic companies at home) and those rates have been declining since 1980 in both advanced and developing economies.

This picture is unlikely to change in the near term. The BEPS Project does not address headline corporate tax rates, which ultimately drive tax competition (although it does address certain tax incentive regimes, including the so-called patent or IP boxes).

And while countries such as Germany and France have called for greater harmonization of rates in the EU, particularly in the wake of Brexit, small member states – Ireland, the Netherlands, Belgium, and Luxembourg – have been more aggressive about using tax policy as a tool to compete for foreign direct investment. And in its 2018 Budget, even France is proposing to reduce its corporate tax rate from 33.33% to 25%.

Apart from competition to attract investment, countries also can be seen as competing to increase their share of taxable income. Countries such as Israel, Turkey and Italy (proposed) have jumped the gun on BEPS Action 1, which is focused on addressing the tax challenges of a digital economy, and adopted a virtual permanent establishment (PE) standard, creating a new form of PE based on a significant digital presence in another country's economy. The UK Diverted Profits Tax ("DPT") and the Australian Multinational Anti-Avoidance Law ("MAAL") seem to be intended as tools to tax profits arising offshore from investments made offshore, which is a change from the normal nexus standards for determining tax liability.

Still other countries (e.g., India through its "equalization levy") have implemented or at least debated new rules to impose a unique tax on the digital goods and services sector. While these unilateral actions are not part of BEPS, the project may have provided inspiration and perhaps cover for governments to propose the more radical changes.[20]

THE CHALLENGES AHEAD

While 2017 was heralded as the year of BEPS implementation, some of the biggest issues are still under discussion, including the digital economy. "While the OECD clearly stated in the BEPS Project that it is not possible to ring-fence the digital economy, some jurisdictions are suggesting that a ring-fence would be appropriate to impose special and different taxes on digital enterprises. As could be expected, this creates significant uncertainties for companies," says Gary Sprague, a Baker McKenzie partner based in Palo Alto.[21]

Multinationals are likely to see more activity in this area as domestic political pressures force the tax policy agenda.

PREPARING FOR THE FUTURE OF TAXATION

As countries throughout the world continue to implement BEPS – often in piecemeal and inconsistent ways – multinational companies will need to take a proactive approach to managing tax risks, which can have a significant, long-lasting impact on their business strategies and brand reputations. Below we identify key strategies to help companies navigate the new environment.

Think global

The heightened cross-border cooperation in tax policy will place greater demands on multinational companies. While regional tax managers have typically overseen local audit activity, that may need to change as governments share information about audits. For example, the position taken on an indirect tax audit in one country may undercut the position taken on an income tax audit in another country. "Multinationals are going to be forced to manage their tax policy much more globally," says Simone Musa, Chair of Baker McKenzie's Global Tax Practice Group.

Be able to tell your story

Companies will face heightened obligations related to their own data. “They are going to need good data about their operations, while also being able to manage that data efficiently and explain what it means in ways that authorities across multiple jurisdictions can understand,” says Kirsten Malm, a partner in Baker McKenzie’s San Francisco office. “Companies also need to ensure that the story they tell Wall Street neatly aligns with what they tell the authorities. And they will need people internally who understand how all of the information fits together.”

> “Multinationals are going to be forced to manage their tax policy much more globally.”
>
> **SIMONE DIAS MUSA**
>
> Partner, Baker McKenzie

This is likely to become an even bigger issue going forward. For example, while CbCR information currently is intended to be shared only among tax authorities, certain NGOs and some politicians in the EU and Australia have called for public CbC reporting. In addition to aggressive transparency initiatives, technological advances are delivering new tools to tax authorities, intensifying the pressure on tax departments and adding to reputational risk.

Engage with stakeholders

Multinational companies should be deeply involved with the ongoing debates over tax policy. This means staying current on what different countries are doing, linking into networks and sharing intelligence, and actively engaging with policy makers.

“The polarizing nature of the debate can put companies in a difficult position with respect to their tax strategies,” says Paardekooper. “They need to be compliant, but they wonder if there is any other moral higher ground that they should adhere to in order to be seen as a good taxpayer.” From a business standpoint, active engagement with the OECD and other stakeholders can lead to improved policies and help to ensure the consistency and proper applicability of the BEPS measures.

Assess the impact of BEPS on your operating structure

The new BEPS guidance will have a significant impact on operating model structures of multinational companies. According to the OECD's status report, BEPS measures already are putting pressure on corporate structures such as "cash box" structures, cost-plus sales and marketing compensation, IP / patent boxes, contractual allocation of residual profit, and treaty shopping structures.[22]

Companies should assess whether their existing supply chains and IP ownership models are compliant with the new BEPS guidance on tax transparency and substance. Companies may also want to consider reassessing the transfer pricing method selection and PE exposure for sales organizations. After BEPS, aligning substance and structure is key when it comes to permanent establishment and transfer pricing risks.

Understand where value is created in your business

More broadly, understanding and identifying the key tax and legal considerations for each part of the supply chain is critical as tax, transfer pricing and legal issues are present at every stage from research, design and planning to buying, manufacturing, distributing and selling. An assessment of the suitability and sustainability of the transfer pricing policy and resulting allocation of profits within a group should consider:

- the economically significant functions, assets and risks
- which party or parties perform the functions, own and operate the assets and assume the risks and
- how non-routine returns are created, such as through the development and use of unique intangibles or the assumption of significant entrepreneurial risk.

> “Companies need to ensure that the story they tell Wall Street neatly aligns with what they tell the authorities. And they will need people internally who understand how all of the information fits together.”
>
> **KIRSTEN MALM**
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> Partner, Baker McKenzie

4

Toward a new era of

DATA PRIVACY AND SECURITY REGULATION

Given that businesses have access to an increasing volume of data, they are faced with the challenge of how to aggregate and analyze that data to make sense of the multitude of undifferentiated data points. The potential to develop business insights from that data creates tremendous opportunities but it also brings significant challenges for companies across all industries. One of those challenges is reconciling the commercial need to structure and analyze data with increasingly complex and sophisticated data privacy and protection requirements around the world.

SOME SIGNS OF HARMONIZATION

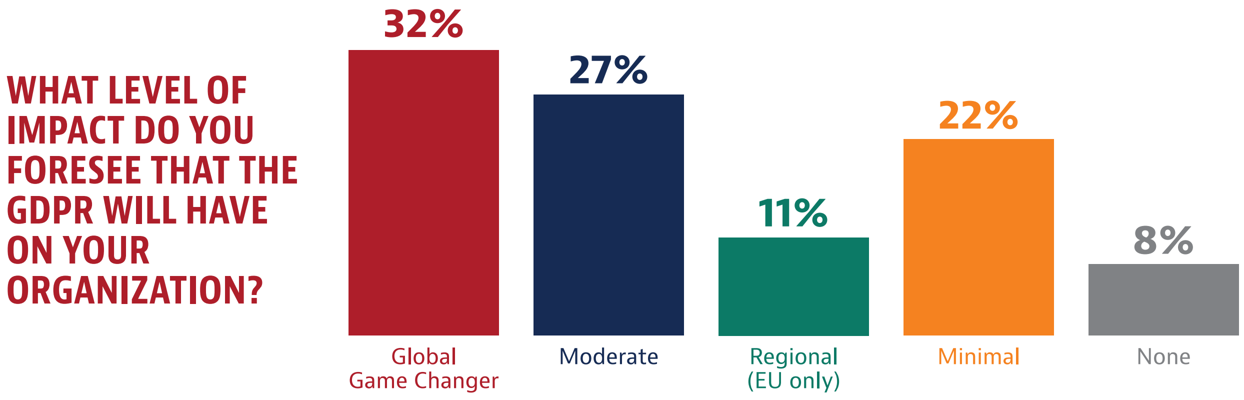
Most data privacy and security laws and regulations around the world are relatively young and largely uncoordinated. As a result, "countries have largely been able to do whatever they want in terms of setting regulatory priorities, and have not worried about limitations on their power emanating from global trading rules," says Brian Hengesbaugh, who chairs Baker McKenzie's Global Information Technology/ Communications (IT/C) Data Security Steering Committee.

While global coordination and harmonization of data protection laws has been limited, in Europe, governments and companies noted the potential effect of privacy laws as trade barriers relatively early and sought to harmonize national privacy legislation with the 1995 EU Data Protection Directive. On May 25, 2018, the General Data Protection Regulation (GDPR) will replace the directive, ushering in a new era of data and privacy protection.

The GDPR will be directly applicable in all EU Member States and has a wide territorial scope: not only will it apply to any company that is established in the EU, but also to any company outside the EU to the extent it processes data in relation to the offering of goods or services to, or the monitoring of behavior of, individuals in the EU. This means that organizations across the globe, once "safe" from the Data Protection Directive's reach, will need to ensure their data protection practices comply with the GDPR — a major compliance task.

With its stringent requirements and high penalties (up to 4% of the worldwide annual turnover of the preceding financial year or EUR 20 million, whichever is more), the GDPR is widely seen as setting the new standard for privacy compliance. It cements and upgrades a wide range of rights for data subjects, including the right to data portability (right to obtain a copy of one's personal data from the controller and have it transferred to another controller), the right to erasure (or "right to be forgotten"), the right to restrict processing and certain rights in relation to profiling. It also raises the bar on standards for consents, cross-border transfers and data breach notification, to name just a few.

According to a Baker McKenzie survey, a majority of data privacy professionals expect that organizations will need to devote more spending and effort to complying with the GDPR, particularly its consent, data mapping and cross-border data transfer requirements.[23]



Source: Baker McKenzie, Preparing for New Privacy Regimes: Privacy Professionals' Views on the General Data Protection Regulation and Privacy Shield

Significantly, like its predecessor law, the GDPR could become a template for data-focused regulation in other regions and countries throughout the world. Argentina, Israel, and Japan, for example, have adopted privacy laws loosely modeled on the provisions of the EU 1995 directive. Switzerland plans to amend its privacy laws to reflect the GDPR standard, and the UK government has confirmed its intent to incorporate the GDPR into national law post-Brexit. "Countries want to be adequate in the eyes of Europe's regulators," says Julia Kaufman, a partner in Baker McKenzie's Munich office, "and they want their companies to be able to do business in Europe."

GDPR is the benchmark for privacy compliance right now and laws in other regions are expected to develop along the same model.

AMID SOME COORDINATION, PROTECTIONISM AND DIVERGENT REGULATION CONTINUE

Notwithstanding some evidence of convergence around GDPR standards, protectionism and divergent regulation continue. The GDPR expressly prohibits companies within and outside the EU from sharing any personal data of EU residents even if compelled by foreign law enforcement or national security agencies, unless permitted by EU law.

Similarly, global harmonization of data protection laws is a long way away. Even within the EU, the GDPR gives Member States ample room to supplement the GDPR by way of national data protection laws. Germany Italy, Ireland and Austria have already passed such a law. Other countries are in the process of drafting and consulting on such laws. Companies looking to bring their data protection practices in line with the GDPR are going to have to navigate through varying and possibly conflicting national laws and GDPR interpretations.[24]

Outside of the EU, data-oriented regulations are largely uncoordinated – reflecting one way in which countries are competing with each other. Countries continue to pursue their own measures, for a variety of reasons (but often to satisfy domestic constituencies). Japan, for example, recently instituted more stringent data privacy rules, and Brazil may be coming forward with its own rules soon.

A range of countries are also enacting cybersecurity legislation, often sector- and jurisdiction-specific. Overall, cybersecurity and geopolitical risks could push more countries to take a more national view of data privacy and protection, with many commentators predicting a clash between governments and companies. What the varied rules have in common is stringency: virtually all of them are placing more and stricter data privacy and protection obligations on companies, while also imposing stiff penalties for violations. This is raising the compliance stakes for companies.

Another example of a national approach towards data protection are so-called "data localization" or "data residency" requirements. These measures either contain outright prohibitions on companies to move their data from one country to another, or throw up costly and time-consuming requirements that have the effect of stifling cross-border data flows. For example, Russia requires companies within and outside of the country to record and store personal data of Russian nationals in databases located on Russian territory and to provide the location of servers to the government agency overseeing telecom and mass communications. Similarly, China's Cybersecurity Law took effect in June 2017 and includes a controversial local data residency requirement that is raising questions and concerns among multinationals operating in China.[25]

"Governments often demand data localization under the guise of protecting privacy, but such laws are really enacted to ease government access to data or to boost local cloud service providers," says Determann. "Data residency laws are anti-privacy laws."

Data residency laws could have a significant impact on multinational providers and users of cloud and other hosted technologies. By dictating where certain data is to be held and processed, local data residency requirements fundamentally counteract many of the benefits of cloud technologies, which inherently involve the sharing, processing and centralizing of data across borders.[26] If more countries go down this path, businesses will need to reconsider their IT architectures more seriously.

THE CHALLENGES AHEAD

With individuals increasingly expecting companies to handle their data responsibly and securely – and legislators and regulators keen to tighten and enforce privacy laws – privacy compliance must become a top priority for multinational companies. Beyond costly fines, the failure to protect data privacy can lead to significant long-term damage to a company's reputation and brand, and the risk goes well beyond losing credit card numbers. Countries throughout the world increasingly require that virtually any security breach involving personal data and a certain risk of harm – even if it doesn't involve social security numbers, health information, or credit card records – be communicated to regulators, the affected individuals and, by extension, the media and public.

These risks are heightened in view of the connection between data protection and human rights. Privacy is a fundamental human right recognized in the UN Declaration of Human Rights, the International Covenant on Civil and Political Rights and in other global and national instruments. As data protection becomes a part of the human rights rubric, the pressure on companies to demonstrate their commitment to privacy compliance will intensify.

"The forces behind the privacy regulation oftentimes are not just about regulating commerce but also about protecting fundamental human rights. Ultimately, investing in good data governance can be a marketing advantage and help build consumer trust," says Dyann Heward-Mills, head of Baker McKenzie's London Data Protection Practice.

PREPARING FOR THE FUTURE OF DATA PRIVACY AND PROTECTION

While businesses realize the value of big data, most would not consider themselves on top of their data mountain. A strategic approach is required, taking into account not only the operational needs, capacities and goals, but also applicable legal and regulatory privacy requirements.

Involve the whole company

Companies need to prioritize data protection and privacy across a range of divisions and departments. It is a critical issue for IT, legal, HR, compliance, communications, investor relations, and the C-suite.

"For many companies, data privacy is somewhat of a hot potato," says Hengesbaugh. "Some will want to treat it as just a legal issue, for the legal department to handle. But the legal department may see it as primarily an IT issue, with the need for systems to be built. And the IT department may say, 'we just put the pipes in place that you tell us to,' in which case it's a business issue. And so the reality is that data is something that now impacts the whole organization."

Work on your comprehensive privacy compliance program

Companies would be prudent to develop, and continually refine, comprehensive privacy compliance programs. "Companies should see the GDPR as an opportunity to rethink their approach to data," says Anne-Marie Allgrove, Global Chair of Baker McKenzie's Technology, Media and Telecommunications Industry and Practice Group.

In addition, while the GDPR is often the best starting point for a comprehensive global privacy program, companies also need to address compliance with other regimes (e.g., California privacy laws, US federal laws such as the Health Insurance Portability and Accountability Act of 1996 and the Fair Credit Reporting Act) which can bear as much or greater risks.

HORIZON SCANNING

Tracking local nuances, derogations and interpretations

. . .

Enforcement and sanctions

Monetary fines, reputational disasters: you lose business and trust. Compliance is not an option — it is a must.

One-stop-shop

Identify and engage with the lead supervisory authority.

Data subjects' rights

What privacy rights should you consider and how?

Profiling & profile-based decision making

Can I profile individuals? May decisions be based on automatic processing?

Consents

How do I secure a valid consent?

Data processors

How do I shape the contract relationship with service providers?

Data mapping

Understand what data you have in house.

Data protection by design and by default

Are privacy rules embedded in my technology and business practices? How do I make privacy a default mode of operation?

Accountability

Be prepared to prove you are GDPR compliant.

Data protection officer

Must have? Nice to have? Or safe to ignore?

Data protection impact assessments

How do I address data processing operations that trigger material data protection risks?

Cross-border transfers

How do I transfer personal data outside the EU?

Data breach obligations

A data breach — what next?

Build your
PRIVACY PROGRAM
as part of your
GLOBAL STRATEGY

DOES THE GENERAL DATA PROTECTION REGULATION (GDPR) APPLY TO YOU? ARE YOU READY?

5

Toward a new era of

LABOR AND HUMAN RIGHTS REGULATION

The expanding web of social and economic challenges that exist throughout the world is stimulating demand for new actions from governments and businesses. In September 2015, all 193 Member States of the United Nations adopted a plan to tackle the most important economic, social, environmental and governance challenges by 2030. At the core of "Agenda 2030" are 17 Sustainable Development Goals (SDGs) which establish important targets for the international community focused on issues such as gender equality, decent work, and good governance.

Notably, this cooperation extends beyond nations to include the business community. The UN Global Compact includes more than 9,500 companies from 145 countries, with 28% of Fortune 500 companies represented. All signatories are committed to aligning their operations with universal principles on human rights, labor, environment, and anticorruption.

Transparency and accountability are central to achieving the SDGs, and businesses are going to face growing expectations in this area as governments, NGOs, the media, unions, investors, and other stakeholders become more vocal in seeking to advance labor and human rights protections within companies and along their supply chains. At the same time, national and local laws to address labor and human rights issues vary widely, posing compliance challenges.

THE COOPERATIVE FORCES INFLUENCING LABOR AND HUMAN RIGHTS

One noteworthy development in the labor and human rights area has been the emergence of greater cooperation among advocacy groups as they press for changes in public policy directed at companies.[28] Trade unions in particular are extending their influence and are partnering with NGOs and other activist groups to build coalitions on issues such as contingent workers, worker health and safety, wages and hours, freedom of association, and collective bargaining.

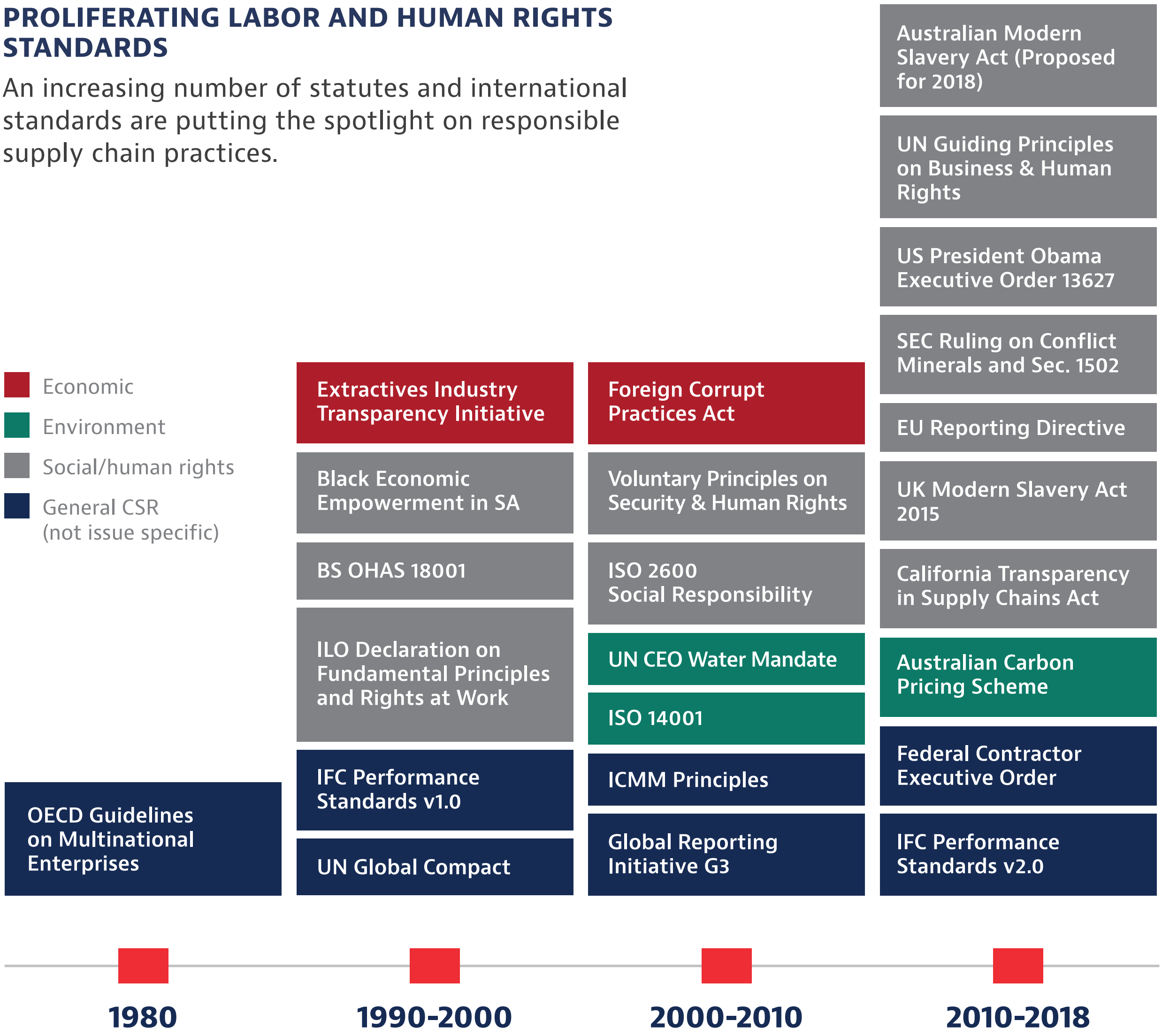
A byproduct of the cooperation among advocacy groups has been a growing focus among investors on environment, social, and governance (ESG) factors. Approximately 41% of US shareholder proposal submissions in 2016 involved concerns about diversity, equal employment opportunity, labor and human rights, and sustainability.[27] Gender pay equity also emerged as a key focus in 2017, with nearly 30 high-profile companies facing shareholder proposals asking them to report on the pay gap between male and female employees and the company's plan to close that gap.[29]

> "National and local legislators are increasingly making CSR-type reporting and disclosure mandatory and holding companies accountable."
>
> **KEVIN COON**
>
> Partner, Baker McKenzie

There has also been a proliferation of measures that place greater obligations on companies to protect labor rights and human rights. “All of this is emblematic of a growing global trend,” says Kevin Coon, a Baker McKenzie partner based in Toronto. “National and local legislators are increasingly making CSR-type reporting and disclosure mandatory and holding companies accountable.”

PROLIFERATING LABOR AND HUMAN RIGHTS STANDARDS

An increasing number of statutes and international standards are putting the spotlight on responsible supply chain practices.



This relatively new type of “transparency legislation” does not require companies to take any specific actions, but rather requires each of them to publish a statement about what steps they have taken. And the information disclosed gives stakeholders the ability to apply pressure and drive change. For example, the Business and Human Rights Resource Centre maintains a public track record of companies’ statements under the UK Modern Slavery Act, with over 2000 statements from companies in 27 sectors, headquartered in 31 countries.[30] As an investigative reporter from The Times noted, this registry is an important tool for journalists to identify companies that aren’t meeting the mark.[31]

Similar forces are converging to focus attention on gender equality and the pay gap. “The topic of gender pay equality is being escalated from various sectors of the organization on an increasingly regular basis,” says Susan Eandi, head of Baker McKenzie’s Global Employment and Labor Law Practice Group in North America. “For the Board and C-suite, it is a highly visible issue that shareholders are demanding be addressed. For business leaders and sales departments, it is a topic on which customers are asking their vendors to take a public position. For marketing departments, it is an avenue to distinguish the company from its competitors. All of those constituencies are clamoring before legal requirements are broached and champions of corporate social responsibility even weigh in.”

DECENT WORK AND ECONOMIC GROWTH

THE NUMBER OF UN GLOBAL COMPACT SIGNATORIES WHO MONITOR AND EVALUATE LABOR RIGHTS PERFORMANCE HAS GROWN TO 53% IN 2017 FROM 44% IN 2008.

Source: 2017 United Nations Global Compact Progress Report

There is longstanding legislation in many countries requiring that men and women receive equal pay for equal work. More recently, the focus in the US, the UK, Australia and Germany has turned to pay transparency, with an increasing number of countries making gender pay information publicly available.[32] Various voluntary initiatives have also been developed, such as the UK Workforce Disclosure Initiative supported by 79 major investors, which ask multinational companies to supply data relating to their direct and supply chain workforce.

“The expectation is that companies will get into a competitive situation in the war for talent—evidence suggests that employees are less likely to join companies perceived as not having tackled this issue,” says Monica Kurnatowska, a Baker McKenzie partner based in London.

GENDER EQUALITY

45% OF UN GLOBAL COMPACT SIGNATORIES HAVE ACTIVITIES TARGETING GENDER EQUALITY

Source: 2017 United Nations Global Compact Progress Report

Moving forward, reporting will become even more mainstream. For example, the newly launched "Action Platform Reporting on the SDGs," co-managed by GRI and the UN Global Compact, is developing a single methodology for measuring and reporting business progress on the SDGs to ensure businesses produce more comparable data.[33]

AMID AMBITIOUS GLOBAL GOALS, VARYING REGULATORY APPROACHES

While coalitions are driving progress on common goals such as the eradication of slave labor and gender equality, legislative approaches vary. As a result, companies are facing a patchwork of laws at the regional, national, and local levels.

In the US, for example, a number of city, county, and state governments have enacted measures aimed at combating gender pay discrimination that are more stringent than current federal law. The measures range from lowering the bar for equal pay lawsuits (by fundamentally altering how equal pay claims are analyzed in court), to anti-pay secrecy requirements, to banning questions about salary history.

These varying legal regulations can make a ''one-size-fits-all" approach impracticable. "Before rushing to undertake studies and publish numbers, employers must understand what is meant by pay gaps in each country. They need to consider not just the message in any narrative they publish alongside their data, but whether this is, or needs to be, consistent with what they are saying elsewhere," says Kurnatowska.

THE CHALLENGES AHEAD

During the next few years there is likely to be growing social and political unrest, coupled with rising concerns about the impact of technology on jobs and workers. These developments are destined to place a spotlight on companies' efforts to advance SDGs, including decent work for all and gender equality.

At the same time, the issue of what constitutes "decent work" is becoming more difficult to answer in the modern economy. Globalization, advances in technology, and growing demand from companies (and many workers) for flexibility have led to a rise in non-standard employment. But there is an increasing debate about the type and quality of work, with the debate intensifying as employment laws and social insurance programs have failed to keep pace with new staffing models.

Going forward, we expect to see more government action and regulation in relation to gig economy workers. For example, the Taylor review in the UK recommends changes in the employment rights of self-employed workers and possibly new definitions of worker status. In the US, some workers' groups are pushing for legislation to charge a fee on gig-economy transactions to help provide portable benefits to workers, with legislation being introduced and drafted in different states.

> The expectation is that companies will get into a competitive situation in the war for talent — evidence suggests that employees are less likely to join companies perceived as not having tackled the gender pay gap issue."
>
> **MONICA KURNATOWSKA**
>
> Partner, Baker McKenzie

PREPARING FOR EVOLVING LABOR AND HUMAN RIGHTS EXPECTATIONS

Labor and human rights issues have risen to the top of corporate agendas, but even the most committed companies can have problems with execution. We offer a few strategies below.

Proactively manage labor and human rights risks

To minimize risks – and create value – companies should develop standards and implementation plans to put labor and human rights principles into operation. Actions to consider include:

- Adopt a global labor and human rights policy stating the company's expectations of employees, suppliers, business partners, and other relevant parties. Make the statement publicly available to internal and external stakeholders.

- Implement a comprehensive due diligence process to identify and assess actual and potential adverse labor and human rights impacts and levels of risk based on geographic scope, rights identification, social responsibility risk, and the legal framework.

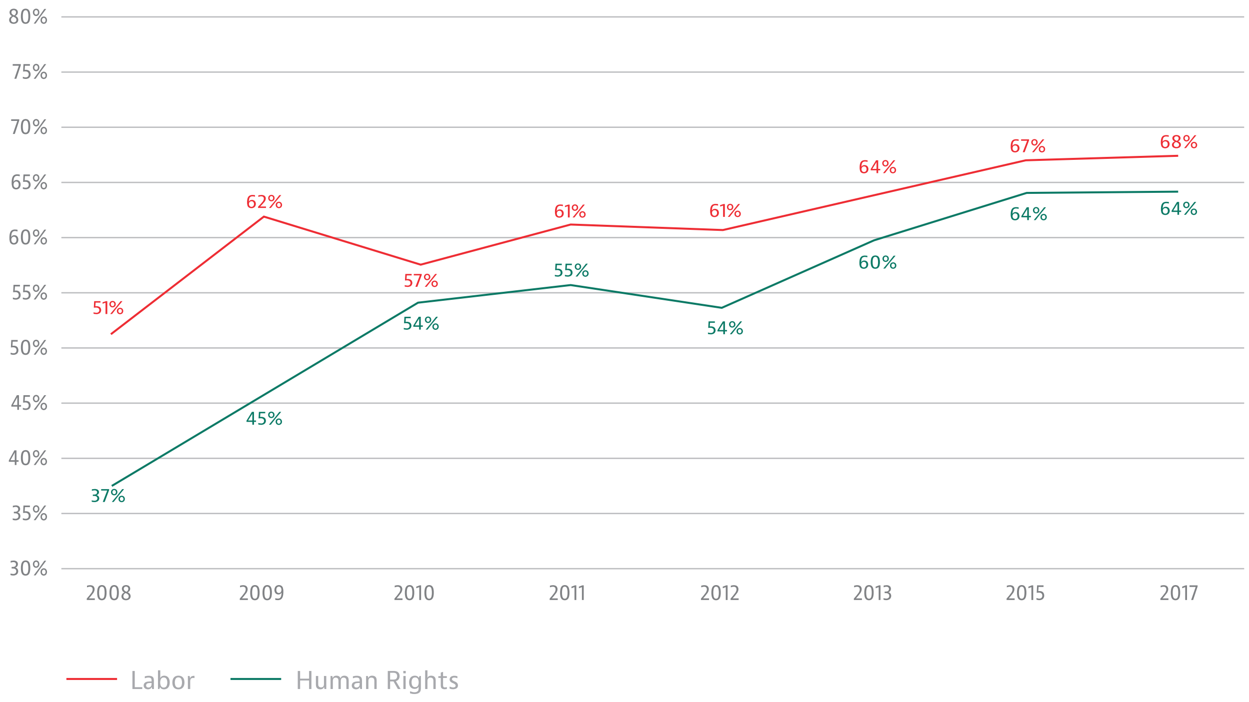
- Ensure the risk assessment is integrated into an enterprise-wide strategy. Assign responsibility for addressing labor and human rights impacts to the appropriate level and function within the company. Make sure operational policies, standards and controls enable the company to identify and respond to those impacts.

- Train board and key staff on how to respond appropriately when situations arise. Consider internal and external reporting to stakeholders about the company's response to labor and human rights impacts to provide transparency and accountability.

- Use qualitative and quantitative indicators and feedback from internal and external sources to assess whether your policies and practices are effective, including surveys, audits and grievance mechanisms focused on labor and human rights practices.

WIDER ACTION: PERCENTAGE OF LARGE COMPANIES

(250 employees or more) with policies and practices that apply to suppliers



Source: 2017 United Nations Global Compact Progress Report

Close the gender pay gap

Gender pay equality can be a challenging topic for organizations, but HR professionals and in-house legal counsel can add real value by understanding the legal landscape and trends and getting ahead of the narrative. Some of the most popular steps companies are taking include:

- Use of pay grades or bands
- Guidance to managers on pay awards
- Review of gender split of salary increases across teams
- Equal pay audit / analysis of equal pay risk
- Recruitment campaigns targeting women

Multinational employers also need to decide whether any action plan could, or should, be a global one. For example, collecting data for diversity monitoring purposes is still an emerging concept and its introduction can even raise suspicions of discrimination. There may also be questions about whether steps to promote female employees will fall afoul of prohibitions against positive discrimination in certain jurisdictions.[34]

Manage misclassification claims

Countries are demonstrating a greater willingness to crack down on the use of independent contractors and/or temporary employees in place of full-time, permanent employees. Misclassification claims can carry significant risks including tax liability, extended employment rights (dismissal protection, leave and severance entitlements, and statutory benefits), pension entitlement and IP rights. To manage these risks, global employers should:

- Carefully structure contracting arrangements, including indemnity provisions
- Treat contracting workforces differently to the employee population – particularly where they are on-site
- Limit use and duration – only use contracting workforces on specific, non-integral activities
- Educate and train managers and use controls to ensure reality matches the commercial terms and
- Audit vendors and supply chains

6

THE PATH FORWARD

Multinational companies throughout the world are facing a more uncertain and more challenging environment today than they have in many decades. Comprehensive trade liberalization is stalled. Cross-border tax strategies are facing greater scrutiny. There's heightened awareness of – and resistance to – the sharing of personal data. And companies are facing growing demands to comply with labor and human rights measures. Many of these challenges are a reflection of the cross-border competition and cooperation that's a defining feature of globalization today.

It's an open question as to whether these challenges will mount or recede in the months and years ahead. And while the solutions will differ by country and by industry, there is a clear hunger for companies to become more transparent. Greater openness is not without risk – it can subject companies to new lines of criticism and inquiry. But it's also an opportunity to demystify their activities and build credibility with customers, policymakers, and civil society.

The broader challenge is as old as globalization itself. The benefits that flow from economic openness tend to be widely dispersed – and thus somewhat opaque – while the downsides are concentrated and plainly visible. Given this longstanding reality, it's incumbent upon multinational companies to actively engage with governments, other companies, their employees, and other stakeholders. That means sharing their frontline knowledge of how global economic integration helps stimulate job creation and reduce prices, while also driving greater efficiency and competitiveness. It's also critically important for companies to help craft solutions for the subset of workers who don't experience globalization's benefits.

A smart approach to public engagement will prepare companies to meet the many challenges that exist across today's business landscape. And that public engagement can help promote an environment that's supportive of what companies do best: create the opportunities that contribute to growth and prosperity throughout the world.

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