

CORPORAÇÕES TRANSNACIONAIS COMO GRUPOS FINANCEIROS

TRANSNATIONAL CORPORATIONS AS FINANCIAL GROUPS

Claude Serfati¹

RESUMO

Embora a atual crise tenha evidenciado as fortes (e devastadoras) inter-relações entre produção e finanças, dando um impulso à abordagem “financeirização”, há a necessidade, quarenta anos após a investigação inicial sobre as empresas transnacionais, de reexplorar a natureza das grandes corporações transnacionais (TNC). Questões a serem explorados incluem a reformulação do comércio internacional e da produção, uma estreita interação entre as empresas transnacionais não-financeiras e (bancários e não bancários) financeiras transnacionais, o desenvolvimento de redes globais, e a força das relações estabelecidas pela maioria deles com “seus” governos. A hipótese básica deste trabalho, que é focado em empresas transnacionais não-financeiras, é que elas não podem ser definidas apenas pelo fato de que são maiores e mais internacionalizadas do que outras empresas. Em nossa opinião, elas constituem uma categoria própria, baseada em uma centralização dos ativos financeiros e uma estrutura organizacional específica (com o papel central na posse da sociedade gestora de participações). Transnacionais, organizadas e estruturadas como grupos de empresas, são um locus de valorização do capital global, onde a valorização produtiva e financeira estão intimamente entrelaçadas. No contexto de um capital financeiro mundial dominado regime macro-econômico de acumulação, a lógica financeira assume um papel preponderante na estratégia das multinacionais. A desregulamentação irrestrita dos mercados financeiros e a multiplicação de inovações financeiras (produtos e instituições) deu um novo impulso para a transformação das empresas transnacionais, que podem ser definidas como grupos financeiros com actividades industriais.

PALAVRAS-CHAVE

Empresas Transnacionais; Grupos Financeiros; Inter-relações entre Produção e Finanças.

¹ CEMOTEV (Centre for the Study of Globalisation, Conflicts, Territories and Vulnerabilities), University of Saint-Quentin-en-Yvelines.

ABSTRACT

While the current crisis evidenced the strong (and devastating) interrelations between production and finance, and gives a boost to 'financialisation' approach, there is the need, forty years after the initial research on transnational corporations, to reexplore the nature of large transnational corporations (TNCs)². Issues to be explored include the reshaping of international trade and production, close interaction between non-financial TNCs and financial (bank and non-bank) TNCs, the development of global networks, and the strength of relationships entertained by most of them with 'their' governments. A basic hypothesis of this paper which is focused on non-financial TNCs, is that they cannot be only defined by the fact that they are bigger and more internationalised than others firms. In our view, they constitute a category of their own, based upon a centralisation of financial assets and a specific organisational structure (with the core role held by the *holding* company). TNCs, organised and structured as groups of enterprises, are a locus for a global valorisation of capital, where productive and financial valorisation are closely intertwined. In the context of a global finance capital dominated macro-economic regime of accumulation, financial logic takes on a preeminent role in TNCs' strategy. Unfettered deregulation of financial markets and multiplication of financial innovations (products and institutions) gave a further boost to the transformation of TNCs, which can be defined as financial groups with industrial activities.

KEY-WORDS

Transnational Corporations; Financial Groups; Interrelations between Production and Finance.

Introduction: tncs, a category of their own

The large weight of large non-financial³ transnational corporations (TNCs) in the world economy is hardly challengeable. According to UNCTAD, in 2008 there were 82000 transnational corporations with a total of 820,000 foreign affiliates. Their aggregate activity is straightforward. The gross product of foreign affiliates worldwide accounted for 10,5% of global gross domestic product (GDP) in 2009, as it reached only 6,6% of the 1990 GDP. In 2009, total sales by foreign affiliates amounted to US\$ 29,2 trillion [UNCTAD, 2010].

At the core of this large web, one can find the top 100 Transnational corporations (hence TNCs) which account for the bulk of all the 82000 TNCs with

² This paper is a revised version of a paper presented to the Cemotev workshop on 'Financialisation of global value chain', October 21, 2010 and to the 2010 Conference of the *European Association for Evolutionary Political Economy*, University of Montesquieu Bordeaux IV, 28-30 October 2010. Thanks to G. Dymski, J. Henry, and an anonymous referee for their useful comments.

³ Non-financial in the meaning given by national account [SNA, 2008, 4.62]: "Nonfinancial corporations are corporations whose principal activity is the production of market goods or nonfinancial services".

their share of foreign assets, foreign sales and foreign employment out of TNCs' total foreign assets, total sales and total employment being respectively 10%, 16%, and 12% [our computation from UNCTAD 2010]. The prosperity of TNCs, despite the current crisis, is hardly challengeable. According to the 2010 Forbes world's leading companies, the aggregate profits of the top 100 most profitable companies reached 803,47 billion \$ (to give an indication France's GDP was 1907 €billion in 2009) .

Despite a steady rise in the number of companies from developing and transition countries in the top largest firms (*Financial Times* includes 124 of them in the 500 largest companies in the world, cited in UNCTAD, 2010), developed countries are overwhelming the top TNCs' scoreboard; with five countries (the United States, the United Kingdom, Japan, France and Germany) accounting for 730 of the top 100 firms [UNCTAD 2010]. Overall, in 2008 TNCs belonging to developed countries accounted for 92% of 5000 top TNCs foreign assets, and 90,9% of 5000 total foreign sales [UNCTAD, 2010]. The weight of large world companies in high tech activities is still more compelling. According to a study released by the European Commission, the top 1400 companies (400 EU and 1000 non-EU), most of them belonging to OECD countries, invested €402 billion in R&D in 2009 (Industrial Research And Innovation, 2010)⁴. This corresponds to approximately 80% of world business expenditure on R&D. The concentration, even among the top world companies is a striking characteristic stressed on in the report, as the top 10 companies account for 13.6% of the total R&D investment by the 1400 Scoreboard companies.

The real influence of TNCs is not evident only by quantitative indicators. They play a decisive role in the reshaping international trade and production, and the strength of relationships entertained by most of them with 'their' governments gives them a critical edge in the world competition. Dismissing claims that globalization means that global companies had become 'stateless', governments and TNCs have understood in this decade the benefits of mutual cooperation in the context of the exacerbation of economic competition, compounded by the financial and economic crisis that has been spreading since the end of 2007 all over the world.

It is the main thrust of this paper that any theoretical examination of TNCs should start from the fact that they cannot be defined, as it is usually the case, only

⁴ Statistical divergences exist between different sources. Jaruzelski and Dehoff report that the top 1000 R&D Companies spent 503 billion \$ in 2009 [Jaruzelski Dehoff, 2010]. They still find a decline in R&D in 2009, due to the economic crisis (-3,5% in 2009 vs -1,9% in 2009 for Industrial Research And Innovation).

as bigger as and more internationalised than other firms. They constitute a category of their own, which requires additional tools to those conventionally used to study 'firms'. Building new analytical tools to understand TNCs was one of the main objectives of S.Hymer, a forerunner in the analysis of the TNC. Dunning and Pitelis recall us that, one of Hymer's lasting contribution as far as the early seventies, was to consider that "*the theory of international operations is part of the theory of the firm*" [1976, p.21; cited in Dunning and Pitelis, 2008]. For Hymer, this entailed radical conclusions on the nature of Multinational enterprises, the scope of their control, power and value capture. Grounding his analysis on a political economy framework, he predicted that the bleak future delivered by capitalism was epitomized by the multinational corporation, which is "*its swan song*" [1972, p. 110]. This puts Hymer's findings a far way from the somewhat conventional 'internalisation' theorist he is sometimes likened to (for a clear recognition by a prominent scholar of cost of transaction that Hymer cannot be identified to a 'left' wing of a coasian analysis, see Teece, 2006].

Forty years after Hymer's seminal inputs, the analysis of TNCs remains dominated by economics' conventional approach to 'firms'. We think that, given their dramatic transformations in the last decade, there is an urgent need for a reassessment of TNCs. Our hypothesis that they constitute a category of their own is supported by many characteristics, including the following:

1) They are organised as groups of enterprises, a reality that has begun to be seriously addressed by statisticians in recent years (see below), while it has been of little concern for theoretical literature. The latter is dominated by issues such as principal/agency relationships (the firm as a nexus of contracts), and cost transactions (the Multidivisional firm as analysed by Williamson is the most efficient and optimal structure).

According to national reporting accounts, the "*statistical definition of enterprise groups*, [is as follows] 'associations of enterprises' bound together by legal and / or financial links which imply control" [Economic Commission for Europe, 2010, p. 4]. TNCs, as groups represent a category of firms of their own, based upon a centralisation of financial assets and a specific organisational structure (with the core role held by the *holding* company). By definition, groups are a structure in which financial control dominates industrial activities. TNCs have long developed financial activities, but they were given further opportunity in the two last decades. Their active management of financial assets has considerably increased in recent

years, challenging once well-established categories (e.g. Foreign Direct Investment, FDIs). Put otherwise, TNCs are financial groups with industrial activities. As such, they represent one modality of contemporaneous 'finance capital', which cannot be defined as it was by Hilferding in the early 20th century as capital industrial that can dispose over only through the banks, putting industry under the dependence banks. [1910, Chapter 14]. In 21th century capitalism, a major characteristic of finance capital is no longer the alliance of industrial companies and banks under the dominance of the latter, but the blurring of frontiers between financial and non financial activities *within* non-financial TNCs.

2) A major feature and a critical edge of TNCs as financial groups lies in their ability to build an *integrated global* space, with financial and industrial operations being addressed in a combined way. It is a *global* space as it overcomes national boundaries and governmental regulations. It is an *integrated* space, as hundred of affiliates (production, R&D, financial, etc.) are *in fine* under the control of central office which manages resources and capabilities with the objective of giving coherence and efficiency to the process of valorisation of capital. Again, we need analytical tools to address the dramatic changes brought about by the creation of an integrated global space, something which cannot be encapsulated within the *internalization* debate.

3) From an economics of production vantage point, this integrated global space can be analysed along a global value chain (GVC) approach [Gereffi, Humphrey, Sturgeon, 2005]. This approach goes beyond the observation of techno-productive sequences; it takes into account the balance of power among GVC's actors, the large connections through which they structure world industries and markets, their mode of governance, the strategy by TNCs to influence the (de)regulation agenda. Finally, a GVC approach draw attention on the category of rent, its source and sharing among the different companies.

The layout of this paper is as follows. Part Two explains why TNCs can be considered as a 'contemporary modality of finance capital'. Drawing on our own reading of Marx, we explore this concept, as it is useful to analyse the global strategy of TNCs. Part three addresses a major feature and a critical edge of TNCs, i.e. their ability to build an *integrated global* space, with financial and industrial operations being addressed in a combined way. Part four shows that FDIs reflects this combination of financial and industrial operations, as Part five shows that intangible

assets, which are largely a creation of the financial community, plays an increasing role in TNCs' financial activities.

Tncs as a modality of finance capital: a theoretical background

Finance capital as concept

A clarification of the concept of finance capital, drawing on our reading of Marx is needed, none the less because it differs or the definition given by the Hilferding's seminal book [1910]. In his major works (*Capital*, Economic manuscripts, Theories of surplus value), Marx puts *Finance capital* in different context and gives it different – although not contradictory - meanings. In some places, Marx refers to finance capital as a specific business - “the trade with money as a commodity” - linked to the specific role played by money in the process of accumulation. “Capitalist function consists exclusively in performing the financial operations for the entire class of industrial and commercial capitalists” [volume 3, chapter 29]. In turn, as capitalism become a dominant form of socio-economic organisation and those operations linked to money become more complex, this business sub-divides in different businesses “Large offices, many bookkeepers and cashiers, far going division of labor, disbursing of money, receiving of money, balancing of accounts, keeping of current accounts, storing of money, etc., all these things, separated from the acts that necessitate these technical operations, make of the capital advanced for these functions a financial capital” [Id.]. In other places or even in the same chapter, finance capital is a synonymous of interest-bearing capital or ‘moneyed capital’, i.e. an accumulation of such claims on production, an accumulation of the market-price, the illusory capital-value [Id.].

A unitary approach to capital is offered by a Marxist framework. Capital, as an abstract category based upon social (antagonistic) relations, finds its concrete form into productive (fixed equipment, etc.) and financial capital, i.e. money capital generating more money thanks to ownership of financial assets and loans, as well as property rights which gives to those monopolizing resources the right to collect rents.

As Finance capital has existed well before the development of industrial capitalism, its modern configuration has its roots in the specific role held by money in capitalism. Capitalism is not an economic (and social) organization based on barter ‘plus’ money, i.e. with money acting as oil lubricating and easing the expansion of commodity exchanges, a view typical of the neoclassical approach

which narrows down money to its function of means of payments. Instead, capitalism is the only mode of production to be driven by a relentless quest of accumulation (accumulate, accumulate!), resulting in more money being collected at the end of the cycle than at the beginning, with money acting as the universal form of value. To phrase it in Marx's wordings, the cycle of capital is M (Money)-P (Production)-M' ($M' > M$), a formula approvingly referred to by Keynes [1971-1989]⁵. In this way, the production (and sales) of commodities, based on the ability for capitalists to accumulate surplus value, is always a means (an intermediate), never the end of the process⁶.

This 'logic' of capitalism paves the way to a growing autonomy of the circulation of money capital, property titles and claims. Autonomy of money capital eased the growth of *fictitious* (interest-bearing) capital, a concept developed by Marx in particular in *Capital*. The market value of this capital is set on the basis of capitalization of the revenues of property titles and claims (for the core role of this category, see Chesnais, 1994). Marx saw the origin of fictitious capital in the development of the credit system and the joint-stock company system (and correlated stock exchanges markets), with the active involvement of government through their public debt. Against the framework of capitalist relations, the vertiginous and autonomous growth of fictitious capital is made possible and gives their capitalist owners the right to extract revenues from value created and existing wealth. Interest-bearing or moneyed capital defines what the essence of

⁵ See "A pregnant observation made by Karl Marx, - though the subsequent use to which he put was highly illogical [was...] that the nature of production in the actual world is not, as economists seem often to suppose, a case of C-M-C', i. e., of exchanging commodity (or effort). That may be the standpoint of the private consumer. But it is not the attitude of business, which is the case of M-C-M', i. e., of parting with money for commodity (or effort) in order to obtain more money". [p.81] Still, the strong differences existing between the meaning for Keynes of this formula and Marx's analysis should not be underestimated, and there has been considerable literature on these issues, see among *alia* Sardoni [1997] .

⁶ Cf « Just because the money-form of value is the independent, tangible form in which value appears, the form of circulation M ... M', the initial and terminal points of which are real money, expresses most graphically the compelling motive of capitalist production — money-making. The process of production appears merely as an unavoidable intermediate link, as a necessary evil for the sake of money-making. All nations with a capitalist mode of production are therefore seized periodically by a feverish attempt to make money without the intervention of the process of production ».

money capital in capitalism is: to produce revenues thanks to its ownership [Marx, 1861-1863].

Economizing the Bohm-Bawerck's 'detour of production', money capital is able to self-valorise through advance of money capital and produce revenues, as "*a pear-tree gives pears*" [Marx, Volume 3, chapter 24, p.2]. Autonomy does not mean independence, instead property titles and claims (finance capital) represents for the most part the social power of private property rights (based on law) to extract value from labour and wealth : "*In so far as we have hitherto considered the peculiar form of accumulation of money-capital and of money wealth in general, it has resolved itself into an accumulation of claims of ownership upon labour*" [Marx, Volume 3, chapter 30]. Capital is based on social relations which gives their owner the right to command labour and to capture some part of the value created in the production and commercialization process. To understand that finance capital resolves *in fine* in accumulation of claims on labour, suffice to think that what is possible for individual units, that is agents and institutions who can be pure rentiers and financial revenues collectors, is quite impossible at the aggregated level – say a country – where value has to be produced by workforce through the labour process.

The very existence of such a duality in capital and its consequences were also later analysed by Veblen, as he was one of the most acute observers of the transformation of capitalism brought about by the incorporation process. In his analysis of the "Modern Business Capital (title of his *Theory of modern enterprises*' chapter 6) he observes that, while "*capital*" as a stock of the material means by which industry is carried on" by the "*received body of (economists') doctrines*", for business, it means "*a fund of money values*" [Veblen, 1904, p. 135] . Likewise, Veblen stated that investments, in industry or real estate, in interest-bearing securities, loans represent "*nothing more substantial than a fictitious duplication of material items that cannot be drawn into the industrial process*" [p.103].

Applying the concept to Tncs

Finance capital is a concept which lost momentum, while financialisation got increasing support [Krippner 2004, Epstein Ed.,2005, for a tentative taxonomy of financialisation literature and its comparison with finance capital approach, see Serfati, 2009] . For those familiar with a Marx-inspired analysis, a major reason for rejecting the former in favor of the latter is because of the seminal definition given by Hilferding, who in famous wordings defines "*this bank-capital – that is, capital in*

money form – which in this way is converted in reality into industrial-capital, the finance capital” [1910]. Notwithstanding Hilferding’s pathbreaking findings, his definition has been criticised for a number of reasons:

- Geographically bounded: even at the time of Hilferding’s writings, the role of commercial banks as provider of money capital was not universal. The point is made by Sweezy [1942] who says that in the United States, private bankers, dealers in domestic and foreign exchange, first entered the field of new securities and in this way gradually evolved the institution of investment banking⁷. Likewise, the British system of finance capital involved a fusion of financial and industrial capital through the practices of the agencies of institutional capital, and was neither bank-dominated nor organised into banking ‘empires’ of the kind depicted by Hilferding [Scott, 1976].

Historically circumscribed: In the three last decades, the irresistible rise of stock markets as a result of market-friendly governmental policies - in mainstream economics wordings, the coming of a market-based replacing a debt-based finance - put banks in a secondary position compared to the role of financial markets in the funding of non-financial corporations.

Others consider that, as the Hilferding’s concept of finance capital should be treated with caution because it does not adequately capture the complexity and range of relations between industrial and banking capital in the course of the twentieth, it is still important because it focuses attention on the organic and institutional links between these two types of capital [Lapavitsas, 2007, p.19].

It is also our view that *finance capital* remains a useful concept for analyzing contemporaneous capitalism. The concept starts from a definition of capital as a certain type of social relations which is incarnated in a distinct way into money and productive capital, and it facilitates the understanding of contemporary capitalism’s structural dynamics. As regards more precisely the nature of industrial groups (i.e. the set of the holding/parent company and its affiliates) following on his research conducted in France in the late 1970s, F. Morin, has proposed to describe them as a unitary structure of governance made up overlapping but hierarchical levels: the financial level which orients and monitors resource allocations (economic level), which encompasses the production (including work organisation, etc.) level ([Morin, 2006]). In an approach which is convergent to Morin’s one, we have underlined the

⁷ Sweezy changed his mind in the mid nineteen’s, observing that a financial superstructure (made up of banks and a host of dealers) was now sitting on top of the world economy and most of its national unit [Sweezy, 1994].

dominance of a financial logic in the strategy of industrial groups; accordingly they can be defined as an “*organisational modality of finance capital*» [Serfati, 1996, p.144].

Finance capital, as a concept, has two facets: one is institutional and the other is functional which. While distinct, they are intertwined [Serfati, 2000]. It is an institutional sector, made up of firms the business of which is based on financial activity (the financial industry as distinct from the automotive, chemical or energy industry), resulting from the division of labor underlined by Marx. It also defines a function, the ability of money capital to produce revenues as ‘pear-tree produces pears’.

These two dimensions of finance capital are conflated in the definition of the financial sector given by national accounts, which is the following: “The financial corporation’s sector consists of all resident corporations and quasi-corporations principally engaged in financial intermediation or in related auxiliary financial activities.” [IMF, 2008]⁸. The definition of financial services has been enlarged to give due weight to the increase in financial services other than the financial intermediation, specifically financial risk management and liquidity transformation. Now, as it is clear from that definition, financial institutions are defined by their main *functions*, which is to provide financial services. This position cannot hold any longer from a finance capital-based perspective. Bank and non-bank financial institutions (mutual, pension, investment funds, etc.) on the one hand, and ‘financial services’ functions on the other hand cannot be conflated because the latter are not performed only by financial institutions, be they banks or non-bank ones.

In contemporary capitalism, this functional opportunity is also offered to industrial groups through the centralisation and circulation of financial assets and other rent-generating assets. They rely on numerous affiliates, no matter the latter are registered as ‘financial’ or not financial units in their home country. One of our arguments with Hilferding’s analysis is that he precisely conflates both aspects, organizational and functional, of finance capital (interest- and dividend-bearing capital). He is wrong to assert that “Through this relationship, Banks ... capital assumes the form of finance capital, its supreme and most abstract expression” [Hilferding, 1981, p. 12]. Although he correctly documents the core role of money

⁸ A slight different definition is by OECD’s definition of financial institutions: «*the set of institutions, instruments, and the regulatory framework that permit transactions to be made by incurring and settling debts; that is, by extending credit*», See <http://stats.oecd.org/glossary/detail.asp?ID=6815>.

capital in capitalism' dynamics (his analysis of money is still close to Ricardo's quantitative theory), he takes granted for universal (in the abstract sense) an institutional configuration which is historically and geographically bounded. Notwithstanding these debates, finance capital remains in early twenty-first century capitalism a powerful concept to both understand the theoretical foundations and provide empirical evidence of the steady and oppressive power of financial assets ownership through the capture of rent revenues (interest, dividends, royalties).

Institutional separation of productive and finance capital

A glaring evidence of the duality of capital (in capitalism, capital-property and capital in production are separated) and the ascendancy of revenues-bearing capital (besides interests and dividends, capital gains, royalties, etc.. belong to a similar category, as they are rents-like revenues generated by the mere ownership of property titles) is provided by the development of *joint stock companies*⁹. The separation in joint-stock companies between the *functions* needed to carry out the production process based upon productive capital and the *ownership* of capital had been evidenced by A. Smith. Smith was mainly concerned by the possibility for managers to 'rob' shareholders¹⁰, even if he saw, according to some comments, some superior organisational efficiency in joint stock companies [Anderson, Tollison, 1982].

Ever since the Berle and Means' seminal findings on the emergence of a powerful class of professional managers insulated from the pressure of stockholders (1932), these issues have triggered a considerable debate in the academic and managerial literature. Sociologists, Lawyers, political scientists entered the debate very early, while mainstream economists turned their attention to this issue only in the 1960s. For the latter, the connection between financial and productive activities within firms goes through inter-individual relations, since the firm is seen as a

⁹ Engels, commenting late in the 19th century on Marx's analysis of joint stock companies, indicated that "*new forms of industrial enterprises have developed, as we know, representing the second and third degree of stock companies*" [Marx, Volume 3, chapter 23]. For him, it was clearly based on the creation of fictitious capital. Commenting on Marx's development of this category, Engels wrote "*This doubling and trebling of capital has developed considerably further in recent years, for instance, through financial trusts*" [Chapter 29].

¹⁰ "*Being the managers rather of other people's money than of their own, it cannot be well expected that they should watch over it with the same anxious vigilance with which partners in a private copartnery frequently watch over their own [...] Negligence and profusion, therefore, must always prevail, more or less, in the management of the affairs of such a company*" [Smith, 1776]

nexus of individual contracts [Jensen, Meckling, 1976]. The need to explore the ‘double nature’ of capital, both as physical and financial asset, their functional interrelations, as a unique object of investigation, was an issue of little concern in mainstream economics, after the ‘Cambridge Capital controversy’ and the convincing inputs by J. Robinson¹¹. A more recent attempt has been made, in particular by Williamson to consider that the M-form corporation reaches a superior efficiency because “it takes on many of the properties of (and is usefully regarded as) a miniature capital markets [1981, p.1554]. Numerous critics have been made on the underlying assumption that internal capital markets do not suffer external capital markets’ failures [Bolton, Schlafstein, 1998] as well as use of Chandler’s historical research to encapsulate it into a cost-of-transaction framework [Lazonick, the whole Chapter 7, 1991].

Marx, following A. Smith, did not ignore either the possibility given to some people to build their fortune on ‘swindling’ and ‘cheatings’¹². Still, he was less concerned with the ‘agency’ problem created by the management-ownership separation than by the theoretical implications for capitalism of capital being separately (and both) productive and revenues-bearing capital. For him, joint-stock companies buttressed the separation between productive and money-capital¹³.

The reason why the issues related to the distinct functions of capital as property (financial assets) and capital in the production process are given precedence over the ‘agency’ problem raised by the institutional separation between shareholders and managers is important to explain here. This duality of capital exists even if it is

¹¹ Regarding financial/monetary realm and the ill-named ‘real’ economy, the one of the production and primary appropriation of value as separated issues has a cost in terms of analysis. As late as the end of 2007, a confident OECD report noted that “*the effect of financial turmoil on total activity stemming from the sector itself is likely to be small*” [2007, p.25]. The reason for such a huge misunderstanding of what was already more than simmering is that, according to the report’s authors the financial sector can be accounted for only less than 10% of the value added in most OECD countries. Money is ‘neutral’, has no other role but on nominal price fluctuation, and finance is seen as an institutional sector as any other industrial one.

¹² The development of joint stock companies “*reproduces a new financial aristocracy, a new variety of parasites in the shape of promoters, speculators and simply nominal directors; a whole system of swindling and cheating by means of corporation promotion, stock issuance, and stock speculation. It is private production without the control of private property*” [Marx, volume 3, chapter 27].

¹³ “*Transformation of the actually functioning capitalist into a mere manager, administrator of other people’s capital, and of the owner of capital into a mere owner, a mere money-capitalist*” [Capital, vol.3, chapter 27].

the same persons who manage and own the firm – or the corporation¹⁴. The existence of finance capital as money generating more money, (that is financial claims producing interest, dividends, capital gains, royalties, etc.) is neither due to the division of labour between shareholders and managers nor to the existence of financial institutions. Put otherwise, *functional* separation between productive and financial capital does not exist because of this division of labour. It is the other way round : institutional separation between different activities and business grew in importance because in capitalism, money is the ultimate form of wealth, into which everything has, at the end of the process, to be transformed¹⁵. That said, no doubt that the evolution of the institutional design of the firms since the mid-19th century, as explored below, considerably helped to reinforce (but not create) the autonomy and ascendancy of revenues (interest, dividends, etc.) bearing capital.

Three main stages in the autonomy of finance capital

The separation between productive and finance capital (revenues-bearing capital) within capitalist enterprises has been growing since the mid-19th century. For the purpose of this article, three major stages are briefly reviewed. The first stage corresponds to the introduction of limited liability in JSCs introduced in England in 1855 after a gradual extension since the repeal of the Bubble Companies Act (1825, passed in 1702, which had sought to prohibit unincorporated joint stock companies and the Bubble Act, under which it became a crime to organize such corporations without explicit royal consent).

In the USA, limited liability began early in the 19th century (New Hampshire in 1816, Connecticut in 1818, Maine in 1823), as New York (1811) and New Jersey (1816) adopted statutes for the incorporation of manufacturing companies that provided for double liability [Blumberg, 2006]. In Japan, JSC spread very rapidly

¹⁴ “The employer of capital, even when working with his own capital, splits into two personalities — the owner of capital and the employer of capital; with reference to the categories of profit which it yields, his capital also splits into capital-property, capital outside the production process, and yielding interest of itself, and capital in the production process which yields a profit of enterprise through its function [Capital, vol.3, chapter 2]

¹⁵ The distinct existence of corporations and their individual owners was confirmed by in the English House of Lords case of Salomon vs Salomon. The court’s decision allowed private actors to organize their business through the corporate legal form, even though the enterprise was composed of the entrepreneur and members of their household alone, and so was not strictly a true joint stock enterprise but a sole trader who would, up to that point, have been personally liable to all creditors [Muchlinsky, 2010]

from the outset of modern economic development, as they were propped up by Government officials, despite businessmen reluctance to adopt this form of modern enterprise [Daito, 1989]. In France, the Code of Commerce of 1807 authorized the creation of sociétés anonymes (corporations), as well as *sociétés en commandite par actions* (limited partnerships). Still, at the turn of the 1880s, for a number of reasons, French entrepreneurship lagged behind other developed capitalist countries. It was only in the 1920s decades that the “*triumph of limited liability came by*” with the number of companies created was two-fold the one before WWI [Bouvier, Caron, 1993, p.774].

The creation of JSCs reflected the structural thirst for capital in some industrial sectors, such as transport infrastructures (canal, railways), public utilities, and obviously the financial industry itself insurance, banking. The process widened to new industrial sectors at the end of the 19th century, including steel, oil and of course banks. As economists have long acknowledged, some industries, based on economies of scale and positive externalities, require monopolization. Still, this leaves again open the precise organizational forms, and this structural impulse for centralization of capital should not be confused with the institutional design adopted by JSCs. Incorporated associations, with public or quasi-public status, performed well in many countries, and when and where (mainly in the USA), it was decided that corporations would be given the status of public utilities, this did not entail introduction of limited liability and creation of holdings [Handlin and Handlin, 1945]. That corporations with limited liability was not an outcome of capitalism *per se* but resulted from complex reasons of which the political ones came to the forefront has long been claimed. As showed by Ireland [2010], the limited liability, low denominations of shares resulted from political pressures aimed at meeting *rentiers*' demands. Ireland concludes that the feat was to give shareholders control rights on the company while exonerating them from personal responsibility for the debt and liabilities of the companies.

The second stage in the development of organizational forms of enterprises reflecting the autonomy of capital as property vis-à-vis productive capital was the creation of holdings. According to a well known definition given by Bonbright and Means a holding company is “any company, incorporated or unincorporated, which is in a position to control, or materially to influence, the management of one or more other companies by virtue, in part at least, of its ownership of securities in the other company or companies” [1969, p.10]. The most influential was in 1899 Jersey

Standard, which while retaining operating functions, became the parent holding company thirty-three corporations. Holdings came to become a major, if not dominant organizational form in the USA.

The dispute regarding the dangers or benefits of limited liability, already vivid about JSC became still more acute with the development of holding companies. That risk-taking capitalism can be exonerated from liability, that rentiers were given increasing momentum was indeed distant from capitalist ideal-type as hoped by some theorists and policymakers. Still, in the case of the extension of limited liability to holding companies, it was not only rentiers who were exonerated from liability, but corporations themselves owning a majority of shares in other corporations, thus insulating the parent's shareholders from "*a second layer of protection*" [Blumberg, 1986, p. 607] . For that reasons, the advantages of limited liability are assessed irrelevant to the 'incredibly complex' special world of corporate groups [Id. p.624]

While *Groups* as organisations, are defined by a hierarchical structure as well as by a strategic and financial control by the head (parent) company, their institutional design spans a range of specificities which could be history- and largely country-dependant [Jones and Khannah [2005] . Arguing against the mainstream view that such structures are inefficient and rent-seeking (in particular as far as they are closely connected to governments) , Khannah, Yaffeh [2007] find that they are not an exception that would result from resistance to 'good governance', but are largely present in many countries outside the United States. Business groups, centered on a family control are a dominant form in many Asian countries [Goto, 1982]. Corporate pyramids are vertically-controlled groups ("pyramids"), and there are horizontally-linked groups, where cross shareholdings are important [Khannah, Yaffeh, 2007]. Likewise, the holding form became dominant in Europe in the post WWII decades, but numerous and different types of relations between holding's parent and their affiliates industrial production-oriented took place in European countries [Amatori, Colli, 2007]. Some differentiate between 'pure' holdings, investment company ("a cousin (sic) of the latter"), corporate pyramids with a corporation acting as holding company at the apex [Banks and Cheffins, 2011].

Finally, despite that differences between holding companies and conglomerates are strongly underlined, including by Williamson [1981] who found that the latter is more efficient than the former, there has been all around the world in the post-WWII decades, a similar trend towards the creation or consolidation of

industrial groups based on centralization of parent companies holding the control through financial assets ('capital-property') of numerous affiliates in charge of production. As the creation of holdings aimed at overcoming industrial constraints (economies of scale, coordination of distinct technical or managerial operations), it clearly reflected foremost a financial centralization, i.e. the centralization of property claims, the objectives of which were to reinforce market dominance and political power of the group, as well as increasing financial wealth for shareholders. In most cases, whichever their national singularities, these different types of industrial groups are defined by strong intercorporate relationships relying on more or less dense equity interlocks, but also tight interpersonal and other informal relationships rather than market-based transactions, with a holding company centralizing and controlling financial assets and designing the strategy of the group as a whole.

The third stage was the development of transnational corporations. The deepening and widening of financial opportunities eased by the radical changes that occurred in the 1980s and 1990s international monetary and financial setting along with shareholder value-based governance dramatically increased TNCs' financial tropism [Lazonick, O' Sullivan, 2000]. The statistical definition of enterprise groups is as follows: "associations of enterprises' bound together by legal and / or financial links which imply control" [Economic Commission for Europe, 2010, p. 4]. Valorization of their assets has become more based on active management and further sophistication made possible by deregulation of financial markets, including products innovations and offshore institutions (for debates on the role of TNCs' financial objectives in the early 1970s, see United Nations, 1973).

The disconnection within TNCs between their financial flows, be they for payments, cash netting, trade finance, loans/debts, cash pooling, etc., and their goods flows is further exacerbated by the creation of hundred, some claim thousands, of Special purpose entities (SPEs), the main purpose is to maximise the profitability of money capital¹⁶ [Sola, 2006]. Other names given to institutions performing similar financial objectives than SPEs include "special purpose vehicles, shell companies, special financial institutions, brass plate companies, mailbox companies or international business companies" [Economic Commission for Europe, 2010].

¹⁶A conventional definition of SPEs by OECD [2008a] is entity "in which the parent companies are resident, and (2) engaged primarily in international transactions but have few or no local operations".

The innumerable SPEs created by TNCs have been keeping up with the centralization of tasks and functions. There is no paradox in having on the one hand a centralisation of control, in particular of financial operations, and on the other hand a decentralization of operations through the creation of hundred of entities dispersed in the world, mainly in low-tax jurisdictions. That does not mean that all these SPEs are registered and classified as financial corporations: the IMF [Sola, 2006] distinguishes between non-financial (shared service centres for administration, marketing, accounting, merchanting, management of patents, etc.) and financial SPEs proper. Most of SPEs are still financial ones (cash pooling centres, Treasury centres, Conduits entities, etc.¹⁷) and in this context, because they are present in different countries TNCs draw benefit from the differences between domestic financial markets or between their different segments.

To shed some light on the financial dimensions of industrial groups, we collected data on the French case. That the group, as organizational structure is designed to drain financial revenues is evidenced by those data (compiled in figure 1). One can observe that while the share of holdings in the overall creation in France of value added and workforce payroll (corresponding to the 'real' activity as it is conventionally called) is quite modest (around 2%), their share is quite essential in interests paid and net financial debt (around 45-50%). Holdings confirm to be a structure (a 'conduit') designed to centralize and drain financial revenues. Groups' holdings are built on a 'reversed pyramid' the basis of which is mainly financial, with a very thin top's production-related activities (figure 1).

¹⁷ A cash pooling system can optimise the use of excess cash and interest yield (by maximizing the return by proper allocation of short-term investments) , reduce interest expense (by minimizing the cost of borrowing by borrowing in different money markets) , and costly intra-company transactions. Treasury centres: Treasury centres are usually in charge of managing the treasury activities of their group (Cash flow and cash position forecasting, Banking and cash management, Liquidity management, Funding management, Risk management) . Conduits entities whose main activity is to raise funds from international markets and lend the proceeds to their group [Sola 2006].

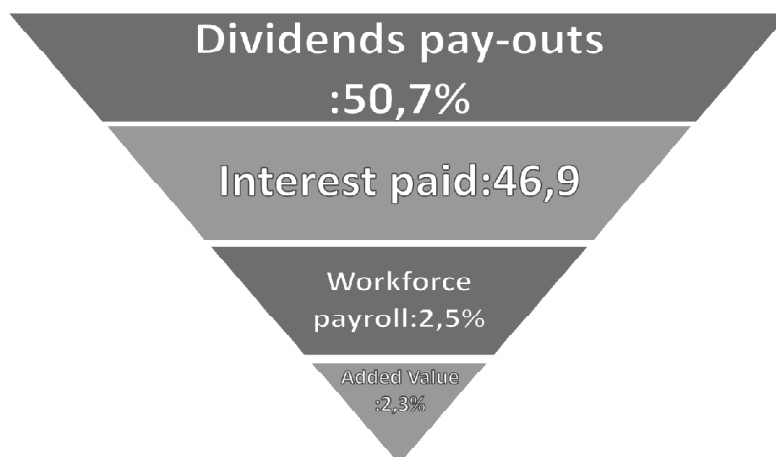


Figure 1: Holdings (Parent companies) of French Non-financial Industrial Groups: The reversed pyramid.

Note: Endettement financier (Net financial debt) : bank debt + security debt

Source: Author's illustration, based on Banque de France database.

A global integrated space

Global valorization of capital

A major feature and critical edge of TNCs as financial groups lies on their ability to build an integrated global space, with financial and industrial operations being addressed in a combined way, a situation remarkably envisioned by Hymer more than forty years ago¹⁸. It is a global space as it overcomes national boundaries and governmental regulations. It is an integrated space, as hundreds of affiliates (production, R&D, financial, etc.) are in fine under the control of central office which manages resources and capabilities with the objective of giving coherence and efficiency to the process of valorisation of capital. To borrow from the conventional industrial and firm's economics, the world is now an 'internalised' area for large TNCs.

This process is in any case, not restrained to the industrial activities of the corporation. As said earlier, it is precisely the blurring of boundaries between industrial and financial activities that reinforces the qualitative distinct features of TNCs as 'firms'.

¹⁸ "The modern multidivisional or conglomerate enterprise [...] appears capable of integrating world production and exchange to a much larger extent" [1970, p.444]. In another paper, Hymer connects financial internationalisation and TNCs, stating that "the multinational corporation and the international capital market should be seen as parallel, symbiotic development" [1972, p.99].

Interactions between productive and financial valorization of capital have become denser, reflecting the “*TNCs global valorisation of capital logic*” [Serfati, 1996, p.148]. We define the logic of global valorization of capital, with two distinct definitions attached to *global*: one by the fact that for large TNCs the world has become a playing field for locating and sourcing their activities and inputs as revealed by the debate about offshoring and two, by the fact that top managers are offered a wide range of modalities for the valorization of TNCs’ financial resources. Hence, valorization of capital could encompass a broad spectrum and have a global reach, with at one end implementation of industrial investments (new equipments, etc.), and at the other end, ‘pure’ financial investments made on financial markets. Between these two ‘polar’ forms of valorization, other ‘mixed’ forms resulting from growing interaction between finance and production take place, blurring the boundaries between the two (financial and productive) ‘spheres’. For example, the development of Intellectual property rights (IPRs) does not reflect only successful innovative activities. It also results from the ability by large TNCs, to capture a share of the value created by other firms, often in Small and Business enterprises (SMEs) and start-ups. This could be made through acquisitions or so-called ‘market power’¹⁹ constraining smaller firms to license their patents [Jaffe, Lerner, 2004²⁰]. It is increasingly acknowledged that IPR has become an object of *financialisation*: the explosion of patents in the last two decades has little to do with a Schumpeterian ‘gale of creative destruction’, rather it evidences that TNCs’ strategy is oriented towards extracting rents, defined as regular flows of IPRs-generated revenues [Zeller, 2008]. Biopharmaceutical TNCs are strongly involved in this strategy [Montalban, Sakinc, 2009].

Overall, we interpret TNCs’ strategies at the era of globalisation in connection with the blurring of the frontiers between value appropriation through

¹⁹ It would be more accurate, as we did elsewhere, to speak of a ‘*relational power*’ held by large TNCs, as the latter reflects their ability to build powerful linkages, many of them being created outside of the ‘market’ and relying on political lobbying, social networks built by executive managers and shareholders, influence on firms of lower size, etc. Market power is an outcome of this kind of power [Mampaey, Serfati, 2006]. That holding corporations are not only economic institutions but also a political power was forcefully claimed by Bonbright and Means [1969, p.6]. Analysing the devastating role of financial institutions, Dymski stresses on the network-based power, and rejecting the narrow approach to market power, argues that ‘concentration’ can no longer stand in for ‘power’ (p.82)

²⁰ See “*An established firm, frequently one whose competitive position and innovative activity are declining, realizes it has a valuable stockpile of issued patents. This firm then approaches rivals, demanding that they take out licenses to its patents*” [Jaffe, Lerner, 2004, p.10].

a direct value-creating production process on the one hand and through rent capture on the other hand. Rent is a complex category which dates back to the very origins of political economy. In our view, rents exist when people and institutions hold private property rights, allowing them to be in a monopoly situation or/and create a (relative) scarcity, from which they can obtain a flow or revenues from other people and institutions in exchange of the use of resources. As a rent could exist because of 'natural' scarcity (ground, natural resources), the extension of private property rights producing a monopoly situation and thus generating rents is a socio-economic embedded process which is endorsed by political institutions (generally State) in charge of enforcement and protection of private property rights.

While the differences between profits and rents were strongly emphasised by Ricardo and his followers, the progressive blurring of their boundaries since the end of the nineteenth century made in reality highly challenging to distinguish between what proceeds from 'entrepreneurial' profits and from rent appropriation.

In the two last decades, there has been a significant broadening of private property rights in new realms of economic and social life (intellectual activity, life process, even pollution has become a sphere for the creation of tradable permits). In that context, TNCs have become more oriented toward the generation of revenues based upon their financial and intellectual property rights than on the production process proper.

Bundle of financial assets and 'slicing up' of the global value chain

Corporations, under pressures from shareholders and 'financial markets' (which is not an invisible hand but made up of quite visible consulting, audit companies, etc.) and as theorized by mainstream economics (in particular the principal-agent one) are now considered as an agglomeration of distinct segments of capital which have to be monitored by their own return on investment (generally shareholder-value oriented). As corporations tend to be seen by financial markets as bundle of assets, the latter have to be highly liquid if they are quickly invested or divested with gains in capital on request on stock exchanges. In the United States, where this radical transformation proceeded initially, large modern corporations came to be run by managers who endorsed the financial conception of control firm [Fligstein, 1990, Chap.6]. Governmental policies financial markets deregulation-oriented, which were implemented in all industrialised countries over the nineties, reinforced this managerial ideology.

It is now conventionally admitted that the wave of mergers during the eighties and nineties was, under the influence of ‘market for corporate control’ approaches, largely finance-driven and that they reflected an underlying shift in the dominant conception of the firm toward a financial model [Davies, Stout, 1992,p.629] .

This short-termist, financial gains-motivated strategy, seems to have been reinforced in the USA by the ‘new finance capitalism’ in which a small handful of mutual funds have become the most significant large-scale corporate owners. They combine the double benefits of concentration and liquidity, resulting in the ownership of vast, but evanescent networks of portfolio companies [Davis, 2008]. Now, that industrial restructuring of their global value chain through external control by stock markets was successful even from a shareholder perspective is challengeable, as almost 70% of mergers failed to achieve expected revenue synergies. Not to speak of their negative effects on labour [Milberg, Winkler 2010, Huws Ed., 2006]. The role of finance in cross-border Mergers and acquisitions was still more evident than in the one confined within national boundaries of developed countries. The conundrum was that the cross-borders M&As wave occurred and persisted during two decades (1980s and 1990s) despite the fact that many of them failed short of delivering the anticipated positive results in terms of both share prices and productivity [UNCTAD, 2000] .

This view of corporations as a set of disposable financial assets has been correlated to dramatic change on the side of the production process. In any case, *a* major goal set by management was to cut down labour costs, refocusing on core competences by dropping non-core activities and maximizing synergies, search of scale economies, cuts in costs through the closure of plants, etc. ‘Vertical disintegration’, divestment of segments of industries’ supply chain, ‘slicing up of the value chain’ are some of the words used to describe the process. Improving the overall efficiency and effectiveness of the firms’ resources, as well as economizing organizational costs assumed to have become higher than market’s transaction and agency costs, refocusing on core competences, priority to scale economies were advocated if these strategies were to be for implemented. A general trend for management has been to drop productions assessed to be insufficiently value creating or/and ‘non strategic’. Practically, ‘upgrading’ by refocusing on the two ends of the global value chain has been the objective coupled with shorter time horizons in investment decisions. This means preserving strategic activities, such

as trans-divisional research, technology and business intelligence, development and design, etc. Managers have also developed strategies focused on the lower end of the value chain, i.e. the final integration of the product (often designed and described as a 'system') which is high margins- generating through branding, marketing, protection of intellectual property, etc.

Restructuring on the production side and quest for financial revenues are interrelated. They result from the ability for large TNCs to act on a global integrated space is also underlined by Milberg, who shows that Global production strategies have helped to sustain financialization [2008, see also, Palpacuer, 2008].

Intra-TNC trade and transfer pricing

The restructuring of GVC and the fragmentation of production processes within global value chains are mirrored by the growing international sourcing of intermediates. The share of intermediate manufactured products in non-fuel world trade was around 40 per cent in 2008 [WTO 2010, p. 2]²¹. Trade in intermediate inputs (primary goods, parts and components, and semi-finished goods) takes place mostly among developed countries and represents respectively 56% and 73% of overall trade flows in goods and services over the 1995-2005 period [Miroudot, Lanz, Ragoussis, 2009].

This large development of intra-company trade is largely an outcome of outsourcing and offshoring, two processes which dramatically affected the organization of GVCs. Still, these trade flows give support to financial flows, or to be more precise, the distinction between trade and financial flows has become more challenging, as the next sections on FDI and Intangible assets evidence it. To sum up, the Intermediates trade is in a large part an intra-TNCs trade. TNCs have been able to increase their grip thanks to network networked forms of organization and coordination, allowing them to capture part of value added created in institutions participating to those networks (small and medium sized firms, public research centres, etc.). The development of an integrated space is evidenced by the large

²¹ Of course, statistical data reliability on the volume of intermediates traded on a world scale has to be improved. The 2008 WTO report notes that because each time goods cross the frontier, an international transaction is recorded, the compilation of merchandise trade statistics by customs administrations results in the recording of these goods more than once. The impact of this "double counting" can be significant, with the international supply chains which include a number of tasks – as is the case for transport equipment and electronics – resulting in that unfinished goods may cross frontiers several times during the assembly process

share of intra-TNCs trade in the world trade. According to OECD data, in 2006, export propensity by affiliates under foreign control in the manufacturing sector was almost 100% in Ireland, 60% in Finland, almost 40% in France, and only 10% in the USA [Hatzichronoglou, 2010]. Even if it is difficult to collect robust measures on that process, according to some estimates, 60% of the world trade consists of internal transfers within multinational companies [Sikka, 2009].

Not surprisingly, intra-trade is a support for profit shifting and transfer pricing (TP). Profit shifting is anything that affects the profits that are subject to the corporate income tax [Huizinga, 2009]. Estimates of the revenue losses from corporate profit shifting vary substantially. In the US, where the research is by far the most advanced, estimates range from about \$10 billion to about \$60 billion for US corporations [Gravelle, 2009]. In France, opportunity given to TNCs by a steady decline of capital controls has been so large that, according to a study released by the *Conseil National des Impôts* (National Council on Tax), in recent years large companies paid less taxes in proportion of their revenues than other companies [Conseil des prélèvements obligatoires, 2009]. One of the reasons might be the massive location of French TNCs' affiliates in tax havens. There were in 2009 1470 entities created by the 39 blue chips, that is 14% of all their foreign affiliates [Chavagneux, Rinuy, 2009].

Mainstream economics addressed transfer pricing following the Hirshleifer Rule [1956] : where and when an external market price exists, the TNC's efficient transfer price should be the external market price. The main critic is that the integrated global space designed by TNCs means that affiliates are under the centralised control of the parent company. Put otherwise, intra-TNCs relations (exchanges of resources, financial flows, management of workforce, implementation of property rights, etc.) are *by essence* distinct of those existing on an (hypothetic) (external) free market, allegedly ruled by 'arms-length' relations between individual and equal agents. A second critic to the mainstream TP approach is the difficulty to precisely measure an 'arms-length' price, to which transfer pricing could be compared. A growing share of intra-TNCs trade is made of intermediate inputs, largely intangibles, for which it does not exist a pure competitive market with comparable products.

TP is central in TNCs strategies. They offer an elegant and opaque way to meet their financial goals. The latter include managing cash flows, supporting R&D, funding capital expansion, paying interest on debt, meeting tax liabilities in accordance with overall group tax strategies and funding dividend payments to

shareholders [PricewaterhouseCoopers, 2009]. Intangible assets gives a serious opportunity to TP policy by TNCs, as said in a subliminal advise by consulting “It is not necessary that the asset appears on the balance sheet for it to have significant value for transfer pricing purposes” [PricewaterhouseCoopers, Id. , p.47].

Surveys of top TNCs reveals that management is fully aware of the very importance of TP. Transfer pricing is the single most important issue for 76% of parent respondents in the pharmaceutical sector, an increase of 19% compared to a similar 2005 survey. Pharmaceutical companies are nearly twice as likely as companies in any other industry to experience an adjustment of transfer prices, and parent respondents in the pharmaceutical sector said that 56% of transfer pricing examinations since 2003 resulted in adjustments [Ernst&Young, 2009].

Simple in its principle, TP represents a real challenge for regulatory authorities (e.g. OECD 2010). The strict application of the ‘arm’s length principle’, as said earlier, is often problematic in practice. This explains the magnitude of financial flows generated through TP practices. On the basis of trade statistics, it is estimated that the scale of manipulated transfer pricing in trade only to and from developing countries amounted to roughly 500 US\$ billion in 2006, that is 6,5% of their foreign trade, and almost 50% of their total capital flight [NOU, 2009].

Foreign direct investment at the crossroads of production and finance

Industrial strategies have driven the dramatic restructuring of their GVC by TNCs that took place in recent years. It is only a part of the story as financial objectives are clearly present in GVC restructuring. In particular, outsourcing through contract manufacturing or any other form is also motivated by ‘international tax avoidance’ [Gravelle, 2009].

The strong rise in the flows of Foreign Direct Investments (FDIs) (in absolute terms or in proportion of GDPs) is seen as an evidence of the globalization of production process, reflected in the development of offshoring. They are given a different status from Foreign portfolio investments (FPIs) , which are seen as reflecting more short-term, financial objectives, as they are in general carried out at least in emerging-market equity by large mutual funds and privately held hedge fund [Global Development Finance, 2004]. That FPIs have little to do with productive issue is confirmed by a recent study which finds that they are used as a tax evasion device: 2/3rd s of all US FPI is hidden from the authorities, and conversely US FPI is more than two and a half times as large as one might suspect on the basis of official

figures [Dharmapala and Hines, 2009]. This finding is confirmed by an IMF's research, stating that huge discrepancies exist between portfolio assets and liabilities in selected offshore centres. Portfolio assets held by foreigners in Luxembourg to be worth US\$1.5 trillion at the end of 2008; while portfolio investment liabilities reported by the government stood at US\$2.5 trillion [Lane, Milesi-Ferretti, 2010]. A black hole indeed...

Even for FDIs, things are not so clear. Indeed, their real meaning as productive investments is questioned, while the play of financial motivations in FDI operations is addressed [Forssbäck and Oxelheim, 2008]. Some literature has for years drawn attention on the status of cross-border Mergers&acquisitions (M&As), which account for over 80% of FDI between developed countries, and for over 40% of FDIs from Developed to developing countries [Unctad, 200]. M&As do not add – and often subtract – manufacturing capacities, they only involve a change in ownership, and as such they should distinguished from 'Greenfield' (creation of industrial capacities) or 'Brownfield' (increase in existing of industrial capacities) Investments. M&As reflects the need to carefully distinguish between ownership of capital (and change of) and productive activities (the 'double nature of capital'), evidencing the extent to which large corporations can carry out their productive and financial (control of ownership) objectives.

Thanks to painstaking research and discussion among statistician accountants that have taken place for years, it has increasingly become evident that large segments of FDI foremost reflect financial activities by TNCs. Flows of FDIs are fed by three components: equity, reinvested earnings, intra-company loans. A 2004 World Bank report underlined that intercompany loans and reinvested earnings were often used in 1990–2002 as a means to adjust FDI. Once considered as quite distinct from Foreign portfolio investment (FPI) seen as more short-term- and financial-oriented, FDIs have gone through strong volatility in the 1990s, especially intercompany loans and reinvested earnings, which were nearly as volatile as debt flows. [World Bank, 2004]. The report listed factors affecting the composition of FDI which are mainly financial-relevant (tax costs, ownership control, investment regulation), the macroeconomic environment being another factor.

More recently and in the same vein, a report commissioned by the French government claimed that "*Direct investment reflects the intra-firm financial*

activities”[Fontagné, Toubal, 2010, p.14] because most of the three funding components (equity, reinvested earnings, intercompany loans) are classified as generating direct investment, even when their purpose has nothing to do with creation or acquisition of physical capacities of production (fixed investment) but is purely financial (transfers of funds for fiscal engineering, higher rate of return offered in some countries, etc.) .

Based on a reassessment of inter-company loans and a new methodology recommended by the OECD [2008a], data compiled by statistical institutions on FDIs offer stunning conclusions. Basically, data are adjusted by reclassifying intercompany loans according to the country of residence of the ultimate controlling parent of the group. The conventional directional principle on which FDI statistics are compiled is extended to lending between fellow enterprises (defined as entities with no direct links). The recommended rule is that lending and borrowing between resident entities of a resident group and foreign fellow enterprises must be recorded as outward FDI and, conversely, lending and borrowing between resident entities belonging to a non-resident group and foreign fellow enterprises must be recorded as inward FDI.

In the case of France, thanks to research based on the new methodology - that is reclassifying intercompany loans according to the country of residence of the ultimate controlling parent of the group - figures on inward and outward FDIs become quite different. This greatly reduces the importance of countries, such as Luxembourg, that are known to host large numbers of SPEs as sources or destinations of FDI. In 2007, the first country investing in France...was France, which accounted for 26,1% of total inward investments [Terrien, 2009/2010]. Two observations emerge. One, France ranks as the leading ultimate investing country in France in 2008 because of the investments of non-resident subsidiaries of French groups in their French subsidiaries in the form of equity capital investments or reinvested earnings. Two, French TNCs’ intra company loans reached a as high as 39,6% of total inward FDIs, reflecting the scope of intra-affiliates financial flows. There is little doubt that the case of France is not different from most developed countries.

As it is a step forward in attempts to trace cross-border TNCs’ flows, the reform in FDIs’ account methodology is a far cry of exhausting all the channels used by large world corporations, e.g. the OECD’s recommendations do not apply to equity capital transactions between fellow companies. That means that if a

Luxembourg holding company of a French group injects funds into its direct subsidiary, which is also resident in France, this transaction is recorded as inward FDI, even though the ultimate controlling entity is a French TNC. Further research is needed in order to better trace TNCs' strategies.

Intangible assets: unidentified and... in large part, non locatable

A new generation of fictitious capital financial-markets generated

This is not the place here to develop the hypothesis, addressed in previous research, that intangible assets are a creation of financial markets and community. Their considerable swelling over the two last decades reflects to some point their fictitious value²² (or their nature of fictitious capital) [Serfati, 2008]. The rising attraction for the category of intangible assets resulted from the convergence between on the one hand economists, keen to put figures on what they called knowledge capital and, on the other hand the financial community who, from the end of the 1990s onwards, observed of the rising gap between firms' book value and their stock market value. Equipped with this new category, analysts were able to conclude that intangible assets accounted for as so high as over 50% of large companies' stock market value. Put otherwise, intangible assets, for all the vagueness of the concept, account for the bulk of the financial value of top world companies (figure 2) with a decline in their paper value with the 2008 financial meltdown. To give a flavor of the extraordinary increase in the importance of intangible assets, it can be added that they were estimated to account only for 17% of the total stock value of companies in 1975 and 32% in 1995²³.

²² After the wave of 'creative accounting' which thrived in the 1990s, the fictitious nature of the 'value' created by intangible begins to be noticed, even among once-first strong supporters. See this comment posted in a post-financial crisis *Business Week's* paper : "With the stroke of a pen, companies can make themselves appear more financially fit than they are" thanks to "new discretionary accounting rules [which] have made it easier for companies to engage in such behaviour" [Der Hovanesian, 2009]

²³ Source : Ocean Tomo

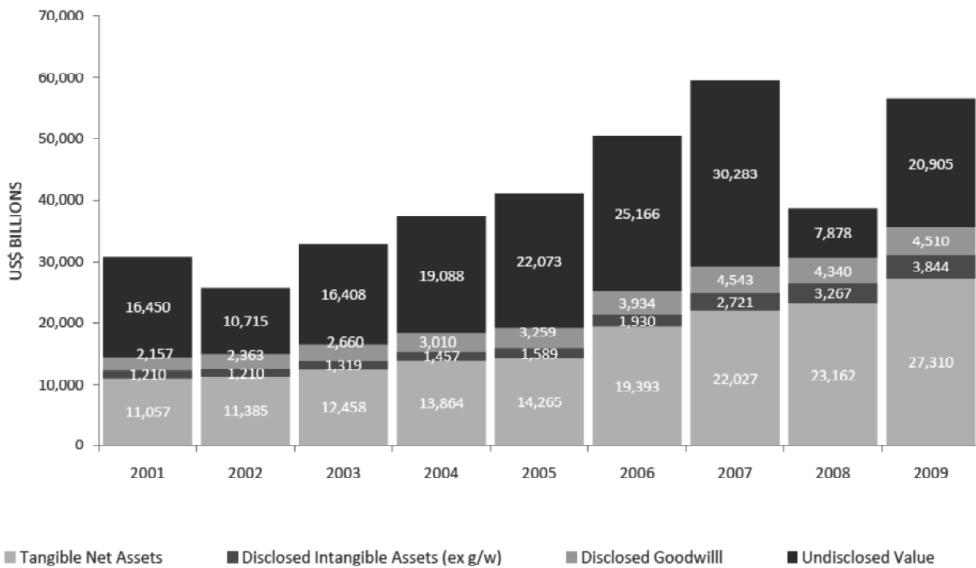


Figure 2: Global Enterprise Value (US\$ billion, 2001- 2009)

Note: According to the 2010 report, the data compile 38,000 companies representing \$56.6 trillion of Enterprise Value (EV) and, in 2009, 99% of total market capitalization.

Source: Brand Finance Global 500 2010

This is not to say that they do not reflect the rise of new inputs and drivers in the creation of value. Intangible assets²⁴ have become a key component of developed countries, and often identified seen as a ‘knowledge economy’. Still, their definition is plagued with great imprecision. There is no agreed definition among economists, neither between accountants, on what intangible assets do mean. It has been found more than 80 approaches or frameworks of value and performance measures [Value measurement, n.d.]. Three core characteristics are generally agreed upon to define intellectual assets: i) they are sources of probable future economic profits; ii) lack physical substance; and iii) to some extent, they can be retained and traded by a firm. The list generally includes at least R&D, patents, and trademarks (OECD, 2008b, p.9). They also include : a) Human capital defined as the knowledge, skills and know-how that employees “*take with them when they leave at night*” (Id., p.10), b) Relational capital which concerns the resources arising from the external relationships of the firm with customers, suppliers and R&D partners, and c)

²⁴*Intellectual*, Knowledge, and in French, *immatériels* assets (or capital) are often alternatively used in the literature as synonymous.

Structural capital which refers to the knowledge that stays with the firm ‘after the staff leaves at night’, e.g. organisational routines, procedures, systems, cultures and databases. The imprecision of this definition is not really improved by others defining organization capital as whatever makes a group of people and assets more productive together than apart, a definition assuming that alternatives would exist for people and society as a whole between producing individually and collectively [Jovanovic& Rousseau, 2001].

In the two last decades, financial markets’ evaluation has increasingly taken precedence over accounting one. Besides disclosed intangible assets (especially when they have been formally protected through trademarks, patents or copyright) , another category has increased in importance, the *goodwill*, defined as the amount above the fair net book value (adjusted for assumed debt) paid for an acquisition, and which account for a significant share of intangible assets, is not informed by companies²⁵. As observed by experts “[our] research shows there is very little disclosure of the nature of goodwill. Only a few companies have provided brief details of what the goodwill is, but this is quite uninformative as it lacks any real analysis or insight” [Intangible Business, 2008]. Goodwill is said to include workforce in place and group synergies, cost savings. Most companies have chosen not to recognize acquired intangible assets separately, but have included them within goodwill. Goodwill is then reported in accounting books (and charged in the income statement).

Finally, ‘Undisclosed Intangible Asset values’, which have no reality, even in companies’ books, make up the bulk of intangible assets. They are defined as “*reflecting the overall premium attached to quoted companies by investors*”²⁶. In more concrete terms, they reflect the mood of the (financial) markets, and when the 2007 financial meltdown began, they were severely discounted.

²⁵ The *International Financial Reporting Standards* IFRS 3, Business Combinations, defines goodwill as follows : “*A payment made by the acquirer in anticipation of future economic benefits from assets that are not capable of being individually identified and separately recognised*” [IFRS 3, paragraph 52].

²⁶ Could they even be ‘disclosed’ to external scrutiny? See a comment by the authoritative *International Accounting Standards Board* : “*Greater transparency in the accounting for intangible assets would potentially undermine the competitive advantage that [...] some entities presently derive from unrecognised and undisclosed (secret) intangible assets that, if presented in the financial report, would cease to provide the level of benefits that would otherwise be expected*”, [IASB, 2007].

Some appealing features of intangible assets

The massive offshoring of intermediate services²⁷, of which a large share is made up of intangible assets, further complicates the compilation of statistics on their cross-border flows for national accounts. A consulting company computed that only for branding, value uplift created by moving the most valuable 500 brands in the world to offshore locations would be \$700bn, a 30% uplift in value and equal to the \$700bn spent by Hank Paulson in his US bank bailout [Brand Finance, 2009].

There are a lot of reasons, besides those usually described as linked to the transformation of the production process and to the rise in the role of knowledge, why trade in intangible has become so trendy. Intangible assets exhibit at least three features which are appealing to TNCs' finance-oriented management and shareholders:

a) As it is self-evident, they have no materiality, they offer opportunities, including profit-shifting (below) and invoices corresponding to transfers of an output the physical reality of which is impossible to trace by external observers²⁸. As noted by a top world consulting company, large TNCs could find an opportunity for increasing the active management of their transfer pricing policy. This construction is useful in the inter-company pricing context when the parent wishes to conduct R&D in several countries but wishes to retain legal ownership of the intangibles (and therefore the profit created by the R&D) in a single country. Contract R&D places the risk in the country that will ultimately own the technology [PricewaterhouseCoopers, 2009].

b) Intangible assets are often shared across TNCs' affiliates, making it difficult to allocate an exact price or/and value to activities. Not only are prices and quantities generally not observed, but most of them can be considered as services produced collectively, and the production of a 'unit' of output is difficult to define. R&D, by its nature, produces unique products, whereas measurement of quantity and prices generally relies on standardized products with prices that are repeatedly observed [Economic Commission For Europe, 2009]. The case of Sun Microsystems is

²⁷ As trade in intermediate products increased in the recent years, trade in intermediate service increase was higher than the one in goods, accounting for over 70% of exports in services [Miroudot, Lanz, Ragoussis, 2009]. The share of intermediate to total trade in services is based on twenty OECD countries for which data on trade in intermediate services is available for the entire period 1999-2005.

²⁸ See: « *Member states encounter considerable problems in getting reliable data about these transactions, particularly when intra-group transfers of R&D results are involved* », [Economic Commission For Europe 2009]

significant [Lynch, Clayton, 2003]. Attempts by UK statisticians to measure the value of software investment activity to be allocated to the country is impossible, because : a) the software developed in Sun UK is used worldwide within the company; b) much of the internal systems software used in Sun UK is written in North America and Asia. In a generalisation of this case, a manager of the UK Office National of Statistics stated that “*any attempt to measure software capital formation accurately in a firm like this - except at the level of the whole enterprise group on an international basis - is likely to fail*” [Id.,p.52]. Again, this difficulty to clearly separate the production – and value – of intangible assets boosts the opportunities for transfer pricing;

c) Their (stock) market value is extremely unstable, paving the way for pure financial speculation. Indeed, intangible assets possess outstanding characteristics of *fictitious capital*, to the extent that their price, as evidenced by their large fluctuations, are less the reflection of ‘real’ value existing within the firm, than the outcome of a *convention* which, as long explained by Keynes in his Theory’s chapter 12, holds so long as people go on relying on the maintenance of the convention.

Once again, TNCs are well-placed to draw benefits of the integrated space they have constituted, compared to the still territorially-bounded national economies. This is clear in the case of taxes, the raising of which is one of the oldest sovereignty’s attributes. There is an agreement on the fact that intangible assets are a preeminent driver in profit shifting and location of capital in tax havens. Industries with a high share of intangible assets, the pharmaceutical and medicine industry and computer and electronic equipment industry set the pace of profit shifting [Gravelle, 2009]. Dischinger and Riedel [2008] find that a decrease of tax rate by 1% raises a subsidiary’s level of intangible assets by 1,6% intangible assets by European multinationals over 1995-2005 period. Likewise, Grubert has estimated that about half of income shifting was due to transfer pricing of intangibles and most of the remainder to shifting of debt [2003].

What is the content of intangible services traded at the international level which ease profit shifting? R&D, software, Intellectual property (patents), accounting and management, marketing, are the main services traded between and within TNCs. Here are two examples:

- A dramatic increase in ‘management fees’. The rise is all the more daunting that the term ‘management fee’ is often used rather loosely to describe any inter-company charge for a transaction that is not clearly either a transfer of tangible property or the right to use an intangible property. The term could include charges

paid for general administrative or technical services or payments for commercial services that are provided intra-group from one or more providers to one or more recipients [PricewaterhouseCoopers, 2009].

- Offshoring and outsourcing or R&D: R&D activities are increasingly offshored and outsourced from contract R&D firms. In the US, the all-industries ratio of contracted-out R&D to company-funded, company-performed R&D increased from 3,7% in 1993 to 7,8% in 2007. For manufacturers, the ratio reached 8.5% in 2007, up from 3,3% in 1993 [NSF, 2010].

Again, because of the immaterial feature of R&D, there is some evidence that geographic separation of the R&D and patent management location could be used by executive managers as a tool to reduce the cost of tax paid by the group ('tax planning'). From that point, it could be tempting for similar objectives, to include activities which are far from meeting what is usually defined as R&D. Conversely, intangible assets are favorably treated in the United States because costs, and are eligible for a tax credit [Gravelle, 2009].

Conclusion

This article has argued that exploring finance-production interrelations in TNCs requires a conceptual framework different from the one which is used to analyse firms in general. By using the concept of finance capital, it has tried to lay out some theoretical arguments on those issues. Further research would help to strengthen those arguments and provide empirical evidence on the differences between TNCs, be the latter due to their nationality or and 'culture', their industrial sector or any other factors.

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