Part I

A view of the landscape

An essay of mine written for the first issue of a new *Journal of International Economic Law* sets out the context of this subject matter and develops some of the policy objectives which influence this subject. The first part of this essay neatly summarizes my views which would introduce this volume. The last part of this essay, by contrast, neatly summarizes some of my current views about the ongoing direction of the world trading system and the WTO. This last part thus provides a nice ending to this volume, and readers will find that at the end of Part VI, so that this single essay becomes the "bookends" to this endeavor.

1 Global economics and international economic law

1. The global economic landscape and implications of interdependence: of stock markets, bananas, and pumpkins

It surprises few people today to see comments about the profound and growing extent of international economic interdependence and linkages. The causes of these developments are numerous: incredible advances in efficiency of communication, extraordinary reductions in transport costs, growing prevalence of instant tele- and cyber-transactions, treaty and other norms causing reduction of governmental barriers to trade, an economic climate more favorable to principles of market economics, cross-border influences of competition which have driven increases in production and service efficiencies, and, last but not least, the blessing of relative peace in the world.

Manifestations of this "globalization" abound: stock market trends that flow quickly around the world; impacts of national government monetary and fiscal decisions; effects of fraud within certain banking or other financial enterprises; worries about health and safety of products moving across borders such as foodstuffs, pharmaceuticals, machinery, appliances; effects of governmental mismanagement and sometimes corruption; worries about the power of nongovernment and private enterprises and their capacity in some cases to operate on the global economy while largely ignoring particular national governmental regulatory protections; and flows of "cultural" influences involving various media often moving swiftly with new communication techniques to transmit music or drama across borders (with substantial economic implications and other effects, even to cause a new taste in Paris for Halloween pumpkins!). A road-map of the various links and cause-effects of a multitude of economic actions becomes an impenetrable maze of pathways, commonly without clear guidebooks to assist their understanding.

Almost every conceivable type of government economic regulation now

* This chapter is based on John H. Jackson, "Global Economics and International Economic Law" (1998) 1 *Journal of International Economic Law* 1–23.

must take account of the international and competitive implications of its activity, and often national government officials feel frustrated at their relative inability to control economic forces that vitally affect their constituents and prevent fulfillment of official goals and promises on behalf of their constituents. Sometimes governments are tempted to utilize their power to influence economic forces to benefit better their own constituents at the expense of other societies (a beggar-thy-neighbor approach). In some of these cases competition among governments to capture such benefits can result in damaging the welfare of all participants – a phenomenon suggesting a "prisoner's dilemma" analysis. One astute experienced political leader has said: "All politics is local."[1] But another astute economic writer has noted: "All economics is international."[2] When juxtaposed, these pithy comments reflect some of the policy dilemmas with which political leaders must grapple.

In recent years, particularly, as the Cold War and its threat of major disaster seems to have receded, there has been much discussion and speech-making about the shifting emphasis from "geo-politics" to "geo-economics" (or some would say to the game of "geo-monopoly"). News media attention has begun to refocus on economic matters, with front page attention given to international trade, legislative initiatives relating to trade, problems of food safety, World Trade Organization (WTO) cases about bananas, the activity of financial institutions such as the World Bank or the International Monetary Fund (IMF), and many other economic subjects relating to investment, competition policy, etc. Scholarly efforts and governmental policy studies have also been giving increased attention to the problems mentioned above. Nevertheless, the careful observer is struck by how much we do not know, and how often scholarship and studies seem only to repeat the obvious or emphasize advocacy of preconceived positions or struggle without adequate empirical data on which to make judgments.[3] Very high government officials have been known to disparage solidly accepted economic wisdom or make statements about legal norms that are misleading or plain wrong. It seems clear to this observer that there is great need and opportunity for reflective scholarly attention to many different systemic and "constitutional" issues about our globalized economy.

The degree to which treaties and international law now appear to "intrude" on national and subfederal government decision-making seems

[1] See Tip O'Neill and Gary Hymel, *All Politics is Local* (1994).
[2] Peter F. Drucker, "Trade Lessons from the World Economy" (1994) *Foreign Affairs* 99.
[3] See, for example, the papers delivered at a conference at Harvard University Center for Business and Government, October 1995 on "World Trade and Services," which discuss the lack of accurate empirical information concerning trade in services.

to support the statements made above. Governments sometimes feel hemmed in, and sometimes object that they cannot take action sought even by their democratic constituencies. The North American Free Trade Agreement (NAFTA) in some respects went very far in its measures seeking national government changes arguably necessary to fulfill the NAFTA international obligations. This was true for the NAFTA investor protection rules, and also in relation to environment and labor standards.[4] World Trade Organization provisions, perhaps particularly those in the intellectual property agreement[5] which require governments to fulfill certain standards regarding their court systems, and also some of the detailed agreements relating to services (especially financial services or telecommunications),[6] appear to insert their rules quite deeply into national legal systems. Of course, one answer to at least some of the criticisms of international rules which operate to constrain governments, is that the global market forces already constrain governments, and sometimes in ways which are not as healthy as the negotiated treaty text.

The remaining parts of this article will explore some particular facets of the problems outlined above. Part 2 will note the importance which significant thinkers and theorists attach to human institutions and the role of legal rules associated with such institutions.

Part 3 will look at the meaning of the phrase "international economic law," noting some of the dimensions of such a subject title, and some of the difficulties for policy, theoretical, and scholarly work focusing on this subject. Part 4[7] will then look at some traditional market economic concepts regarding the role of government action (presumably to enhance the effective working of markets) and suggest how these concepts are affected by globalization and the legal rules of international institutions.

Part 5 will briefly reflect on some attributes and activities of existing international economic institutions, with a focus on the newest and arguably the most important of these, namely the WTO (although most of the discussion could easily apply to other international economic organizations). Finally, Part 6 will examine some of the thinking about future directions of the world trading system and its constitution, and reflect on the implications of those for scholarship on subjects embraced within the broad topic of "international economic law."

[4] North American Free Trade Agreement, entered into force January 1, 1994. See especially chapters 11 and 18, as well as the NAFTA Side Agreements on Labor and Environment.

[5] Final Act Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations, opened for signature April 15, 1994, Marrakesh, Morocco, 33 ILM 1140–1272 (1994) (hereinafter WTO). See WTO Annex 1C, "Agreement on Trade-Related Aspects of Intellectual Property Rights."

[6] WTO, Annex 1C (TRIPS) and 1B (Services).

[7] Parts 4, 5, and 6 of this article are at the end of this volume in chapter 22.

Throughout these parts, however, there is at least one common focus for the discussions found in this article. This is the notion that we are dealing with a form of "constitutional law," involving in this area the broad concept of "constitution" going considerably beyond a written document, and embracing a variety of interconnected governmental institutions as well as evolving practice of many such institutions. The focus is truly the "world trading system," and its legal framework – that which we can here call the "constitution."

2. Markets and governments and the role of law

Whether economic policies which are based on market principles[8] are the best approach for maximizing human satisfaction is, of course, controversial. Various alternatives have been much debated, and many of those largely rejected, but substantial arguments are made in favor of some sort of mixture of policies, perhaps to temper the perceived negative effects of "too pure market approaches." Whatever mixture may appeal to certain societies, however, it seems reasonably clear that markets can be very beneficial,[9] and, even when not beneficial, market forces demand respect and can cause great difficulties when not respected.[10]

Yet even when stressing the benefits of market economics, important thinkers note the importance of human institutions which guide and shape markets. Two Nobel Prize-winning economists stress this proposition. Ronald Coase has stated:[11]

> It is evident that, for their operation, markets . . . require the establishment of legal rules governing the rights and duties of those carrying out transactions . . . To realize all the gains from trade . . . there has to be a legal system and political order . . . Economic policy consists of choosing those legal rules, procedures and administrative structures which will maximize the value of production.

More recently, Douglas North said:[12]

[8] See Richard Lipsey, Paul Courant, Douglas Purvis, and Peter Steiner, *Microeconomics* (10th edn., 1993); Avinash K. Dixit and Barry J. Nalebuff, *Thinking Strategically* (1991); Max Corden, *Trade Policy and Economic Welfare* (1974); Peter B. Kenen, *The International Economy* (1994); and Paul Krugman, *International Economics: Theory and Policy* (1994).

[9] For an overview of the economic principles which support policies of liberal international trade rules, see Alan O. Sykes, "Comparative Advantage and the Normative Economics of International Trade Policy" (1998) 1 *Journal of International Economic Law* 49–82.

[10] See, e.g., James Flanigan, "Turmoil is Free Market Watershed," *Los Angeles Times* (home edition), October 29, 1997, 1.

[11] Ronald Coase, *The Firm, the Market and the Law*, chapter 5. See also C. A. E. Goodhart, "Economics and the Law: Too Much One-Way Traffic?" (1997) 60 *Modern Law Review* 1.

[12] Douglas C. North, *Institutions, Institutional Change and Economic Performance* (1990).

That institutions affect the performance of economics is hardly controversial . . . Institutions reduce uncertainty by providing a structure to everyday life . . . Institutions affect the performance of the economy by their effect on the costs of exchange and production.

Human institutions embrace many structures and take many forms, but it is very clear that law and legal norms play the most important part of the institutions which are essential to make markets work. The notion that "rule of law" (ambiguous as that phrase is) or a rule-based or rule-oriented system of human institutions is essential to a beneficial operation of markets, is a constantly recurring theme in many writings.

With respect to international economics, the world is fortunate to have the advantage of institutions such as the Bretton Woods system (including the General Agreement on Tariffs and Trade, GATT) established through the vision of statesmen, scholars and diplomats at the end of World War II. At least some of the credit for relative peace and economic growth of the past half-century goes to those institutions and their rules.[13] And now, of course, we have a major new organization established on January 1, 1995 in our landscape of economic institutions, namely, the WTO, with an extraordinarily elaborate set of rules.

A critical question almost always asked by anyone confronted with an international law rule is "Why do they matter?" Put another way, there exists much cynicism about the importance or effectiveness of international law rules. Frequently the public can read news of violations of such rules by major and minor nations. In some cases such violations, even when admitted to be such (often there is bitter and inconclusive argument on this question), are rationalized or declared "just" by national leaders. Thus the cynicism about international rules cannot be surprising.

A more careful examination of the role and effectiveness of international rules is necessary, however. First, it should be observed that not all domestic rules are always obeyed either. Yet there are many international rules which are remarkably well observed. Why this is so has been the subject of much speculation[14] which will not be repeated here. Notions of reciprocity and a desire to depend on other nations' observance of rules lead many nations to observe rules even when they do not want to.

At least in the context of economic behavior, however, and particularly when that behavior is set in circumstances of decentralized decision-making, as in a market economy, rules can have important operational

[13] John H. Jackson, *World Trade and the Law of GATT* (1969), chapter 2. At least some credit for over fifty years of relative peace (avoiding a World War III) can be attributed to the reasonably successful activities of the International Monetary Fund and the World Bank.

[14] See Louis Henkin, *How Nations Behave* (2nd edn., 1979); Roger Fisher, *Improving Compliance with International Law* (1981), 12–16; and Abram Chayes, *The New Sovereignty: Compliance with International Regulatory Agreements* (1995).

functions. They may provide the only predictability or stability to a potential investment or trade-development situation. Without such predictability or stability, trade or investment flows might be even more risky and therefore more inhibited than otherwise. If such "liberal trade" goals contribute to world welfare, then it follows that rules which assist such goals should also contribute to world welfare. To put it another way, the policies which tend to reduce some risks, lower the "risk premium" required by entrepreneurs to enter into international transactions. This should result in a general increase in the efficiency of various economic activities, contributing to greater welfare for everyone.

Assuming then that institutions are important, and that law plays a significant role in those institutions, what legal principles can we identify that play such a role? Obviously this can be a vast subject, certainly ripe for scholarly and policy attention of various kinds for years to come. But perhaps one particular principle can here be mentioned, namely the value of a "rule-oriented" approach to the design of international institutions relating to economic activity.[15]

The "rule-oriented approach" focuses the disputing parties' attention on the rule, and on predicting what an impartial tribunal is likely to conclude about the application of a rule. This in turn, will lead parties to pay closer attention to the rules of the treaty system, and this can lead to greater certainty and predictability which is essential in international affairs, particularly economic affairs driven by market-oriented principles of decentralized decision-making, with participation by millions of entrepreneurs. As noted above, such entrepreneurs need a certain amount of predictability and guidance so that they can make the appropriate efficient investment and market-development decisions.[16]

The phrase "rule orientation" is used here to contrast with phrases such as "rule of law," and "rule-based system." Rule orientation implies a less rigid adherence to "rule" and connotes some fluidity in rule approaches which seems to accord with reality (especially since it accommodates some bargaining or negotiation). Phrases that emphasize too strongly the strict application of rules sometimes scare policy-makers, although in reality they may amount to the same thing. Any legal system must accommodate the inherent ambiguities of rules and the constant changes in the practical needs of human society. The key point is that the procedures of rule application, which often center on a dispute settlement procedure, should be designed so as to promote as much as possible the stability and predicta-

[15] See, e.g., John H. Jackson, *The World Trading System* (1997), 109; and John H. Jackson, *The World Trade Organization: Constitution and Jurisprudence* (Cassell Academic, 1998), chapter 4.

[16] See, e.g., North, *Institutions*.

bility of the rule system. For this purpose the procedure must be creditable, "legitimate," and reasonably efficient (not easy criteria).

For example, suppose countries A and B have a trade dispute regarding B's treatment of imports from A to B of widgets. One technique would involve a negotiation between A and B by which the most powerful of the two would have the advantage. Foreign aid, military maneuvers, or import restrictions on other key goods by way of retaliation would figure in the negotiation. A small country would hesitate to challenge a large one on whom its trade depends. Implicit or explicit threats (e.g., to impose quantitative restrictions on some other product) would be a major part of the negotiating technique employed. Domestic political influences would probably play a greater part in the approach of the respective negotiators in this system, particularly on the negotiator for the more powerful party.

On the other hand, a second technique suggested – reference to agreed rules – would see the negotiators arguing about the application of the rule (e.g., was B obligated under a treaty to allow free entry of A's goods in question?). During the process of negotiating a settlement it would be necessary for the parties to understand that an unsettled dispute would ultimately be resolved by impartial third-party judgments based on the rules so that the negotiators would be negotiating with reference to their respective predictions as to the outcome of those judgments and not with reference to potential retaliation or actions by the exercising of the power of one or more of the parties to the dispute.

In both techniques negotiation and settlement of disputes is the dominant mechanism for resolving differences; but the key is the perception of the participants as to what are the "bargaining chips." Insofar as agreed rules for governing the economic relations between the parties exist, a system which predicates negotiation on the implementation of those rules would seem, for a number of reasons, to be preferred. The mere existence of the rules, however, is not enough. When the issue is the application or interpretation of those rules (rather than the formulation of new rules), it is necessary for the parties to believe that if their negotiations reach an impasse the settlement mechanisms which take over for the parties will be designed to apply or interpret the rules fairly. If no such system exists, then the parties are left basically to rely upon their respective "power positions," tempered (it is hoped) by the good will and good faith of the more powerful party (cognizant of its long-range interests).

As the world becomes more economically interdependent, more and more private citizens find their jobs, their businesses, and their quality of life affected, if not controlled, by forces from outside their own country's boundaries. Thus they are more affected by the economic policy pursued by their own country on their behalf. In addition, the relationships become

increasingly complex – to the point of being incomprehensible to even the brilliant human mind. As a result, citizens assert themselves, at least within a democracy, and require their representatives and government officials to respond to their needs and their perceived complaints. The result of this is increasing citizen participation, and more parliamentary or Congressional participation in the processes of international economic policy, thus restricting the degree of power and discretion which the executive possesses.

This makes international negotiations and bargaining increasingly difficult. However, if citizens are going to make their demands heard and influential, a "power-oriented" negotiating process (often requiring secrecy, and executive discretion so as to be able to formulate and implement the necessary compromises) becomes more difficult, if not impossible. Consequently, the only appropriate way to turn seems to be towards a rule-oriented system, whereby the various citizens, parliaments, executives, and international organizations will all have their inputs, arriving tortuously at a rule which, however, when established will enable business and other decentralized decision-makers to rely upon the stability and predictability of governmental activity in relation to the rule.[17]

The degree of desired flexibility for rules is a subject discussed by important writers, sometimes with a suggestion that certain rules be raised to "constitutional status" and embedded in national legal systems.[18]

With these "policy-building blocks" in mind, we can now turn to several other dimensions of the subject of international economic law.

3. Understanding international economic law

It is appropriate to ask what we mean by "international economic law." This phrase can cover a very broad inventory of subjects: embracing the law of economic transactions; government regulation of economic matters; and related legal relations including litigation and international institutions for economic relations. Indeed, it is plausible to suggest that 90

[17] Adapted from John H. Jackson, "Governmental Disputes in International Trade Relations: A Proposal in the Context of GATT" (1979) 13 *Journal of World Trade Law* 3–4 and John H. Jackson, "The Crumbling Institutions of the Liberal Trade System" (1978) 12 *Journal of World Trade Law* 98–101; John H. Jackson, *The World Trading System* (2nd edn., 1997).

[18] See, e.g., Ernst-Ulrich Petersmann, *Constitutional Functions and Constitutional Problems of International Economic Law* (1991). Professor Petersmann has also written profoundly on this theme in some of his other numerous writings. See also Thomas Cottier and Krista Nadakavukaner Schefer, "The Relationship Between World Trade Organization Law, National and Regional Law" (1998) 1 *Journal of International Economic Law*; and Ernst-Ulrich Petersmann, "How to Promote the International Rule of Law? Contributions by the World Trade Organization Appellate Review System" (1998) 1 *Journal of International Economic Law*.

percent of international law work is in reality international economic law in some form or another. Much of this, of course, does not have the glamour or visibility of nation-state relations (use of force, human rights, intervention etc.), but does indeed involve many questions of international law and particularly treaty law. Increasingly, today's international economic law (IEL) issues are found on the front pages of the daily newspapers.[19]

To some extent IEL can be divided into two broad approaches which cut across most of the subjects embraced by IEL. These approaches can roughly be termed "transactional" or "regulatory." Both have their place, but activities of research and policy formulation can be substantially different, and should be understood.

Transactional IEL refers to transactions carried out in the context of international trade or other economic activities, and focuses on the way mostly private entrepreneurs or other parties carry out their activity. Much of the literature, for example, is descriptive. It can be valuable as instruction for potential players, to show "how to do it," and warn against pitfalls. It can also go further and make suggestions for change.

Regulatory IEL, however, emphasizes the role of government institutions (national, local or international). Although it can be argued that the international trade transaction is the most government regulated of all private economic transactions (usually requiring at least a report for each transaction, e.g. a customs declaration), nevertheless, most traditional attention to IEL has been focused, perhaps for practical and pragmatic reasons, on transactions. Yet arguably in today's world the real challenges for understanding IEL and its impact on governments and private citizens' lives, suggest a focus on IEL as "regulatory law," similar to domestic subjects such as tax, labor, antitrust, and other regulatory topics.

But apart from its breadth, what are some of the characteristics of IEL which, for example, might affect the approach to it of scholars or policymakers? The following are some tentative ventures to explore these characteristics, but they are obviously by no means complete.

1. International economic law cannot be separated or compartmentalized from general or "public" international law. The activities and cases relating to IEL contain much practice which is relevant to general principles of international law, especially concerning treaty law and practice. Conversely, general international law has considerable relevance to economic relations and transactions. It is interesting, for

[19] A more elaborate version of some of these thoughts is expressed in John H. Jackson, "International Economic Law: Reflections on the 'Boilerroom' of International Relations" (1995) 10 *American University Journal of International Law Policy* 595–606.