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Judicial Politics and International Cooperation

From Disputes to Deal-Making at the World Trade Organization

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Chapter One

Introduction

This book aims to assess whether, and if so how, judicial politics in the World Trade Organization (WTO) affect the dynamics of lawmaking through multilateral trade rounds. The institutional structure of the international trade regime performs both a legislative function in the form of recurrent multilateral trade negotiations and an adjudicative function through the dispute settlement mechanism (DSM). With regards to the former role, the WTO provides a forum for bargaining and agreeing upon new rules and commitments for the multilateral liberalisation of international trade. With regards to the latter role, the WTO possesses the necessary enforcement mechanisms to foster compliance with any rules that have been agreed. While the WTO increasingly seems unable to steer a way towards broad multilateral trade deals to bring down tariff and non-tariff barriers to trade, the DSM is widely regarded as a well-functioning mechanism, one that largely fosters compliance with existing multilateral trade rules and acts as a buffer against protectionist policies. The multilateral trade regime has, thus, evolved in two distinct ways over the last two decades: legislative trade liberalisation has weakened, while judicial trade liberalisation has strengthened.

The remarkable decline in the WTO's ability to deliver negotiated trade liberalisation has certainly contributed to making judicial trade liberalisation more central to the multilateral trading system. As the members of the multilateral trade regime have found it more and more difficult to find common ground in the setting up of new multilateral commitments for the liberalisation of international trade, the judicial arm of the WTO has gradually become more prominent in advancing trade liberalisation. While this 'conventional' explanation for the rise in judicial trade liberalisation is plausible and has merit, we believe that understanding the current WTO's inability to perform its legislative functions also requires a systematic investigation of the reverse causal pathways between a stronger enforcement of rules and the politics of lawmaking through multilateral trade deals.

While arguments belonging to the 'conventional' camp abound, such reverse causal pathways have surprisingly received only scant attention. Since the creation of the WTO in 1995, the so-called politics of WTO dispute settlement have been the subject of a rich and growing body of scholarly literature. However, we believe our knowledge of judicial politics in the WTO remains far from comprehensive. More specifically, while we seem to know a lot about how the WTO dispute settlement mechanism works, the existing literature has overlooked the less visible, but perhaps more important, question of whether, and if so how, the creation of strong enforcement mechanisms has influenced cooperation among the members of the multilateral trade regime. Has the strengthening of the enforcement mechanisms

of the WTO decreased the likelihood that the members of the multilateral trade regime will reach multilateral trade agreements?

In this book, we address this question starting from the core assumption that policy can be understood as the result of calculated choices made by political and economic actors. When considering the impact of judicial politics on the WTO's ability to perform its legislative functions, we thus believe in the necessity of looking into how judicial politics interact with the trade-related interests of domestic actors, by affecting their preferences, resources, and incentives to mobilise politically and demand that governments act on their behalf. Hence, this book investigates three broad and interrelated issues: (1) the impact of judicial politics on the preferences of the WTO members' trade-related domestic actors in relation to agreements for the reduction of tariff barriers to trade; (2) the impact of judicial politics on the preferences of the WTO members' trade-related domestic actors in relation to agreements for the harmonisation of regulatory barriers to trade; and (3) the impact of judicial politics on the organisational format of the representation of domestic trade-related interests. The central claim of this book is that the judicialisation of the WTO has influenced the domestic politics of WTO members in systematic ways and ultimately has affected their willingness and ability to further pursue multilateral trade liberalisation in the form of broadly negotiated multilateral trade deals.

The legislation – adjudication nexus in the WTO

Our analysis starts with the simple empirical observation that a fundamental tension currently characterises the multilateral trade regime. In 2009, on the eve of the fifteenth anniversary of the creation of the WTO, the Director General of the WTO Pascal Lamy declared,

> [T]he WTO earlier this month reached the milestone of having the 400th trade dispute brought to the body's dispute settlement mechanism. … This is surely a vote of confidence in a system which many consider to be a role model for the peaceful resolution of disputes in other areas of international political or economic relations. … The dispute settlement system is widely considered to be the jewel in the crown of the WTO. … Members agree that, as the bedrock of the multilateral trading system, the dispute settlement system will not be subject to any seismic shift in its fundamental structure as a result of the Members' deliberations (WTO 2009).

As this quote nicely summarises, with the establishment of the WTO in 1995, members of the trade regime created a quasi-judicial mechanism for the enforcement of rules that, by any standard, can be considered highly successful. Of course, this system has not been impermeable to problems and critique. As the famous disputes on the European Union (EU)'s bans on imports of genetically modified crops and hormone-treated beef, or the dispute on United States (US) cotton subsidies, have shown, a few WTO disputes have proven

particularly intractable; these are highly politicised and the source of both heated domestic political debates and diplomatic tensions. Yet, despite these notable exceptions, the DSM of the WTO has been remarkably successful as an enforcement mechanism of existing multilateral trade rules.

For all these successes, however, the emergence of judicial politics as a central feature of the multilateral trading system has gone hand in hand with a steep decline in the WTO's ability to deliver negotiated trade liberalisation. As Goldstein and Steinberg (2009: 218) nicely put it, 'for those favouring rapid and deeper liberalization, the WTO's biggest contemporary problem is an inability to gain consensus on a negotiated outcome. Stalemate in multilateral trade negotiations is the order of the day.' Despite the absence of strong enforcement mechanisms for rules, the General Agreement on Tariffs and Trade (GATT) system was very successful in fostering bargaining processes for the elimination and/or reduction of barriers to trade among the members of the multilateral trade regime. In the period spanning the adoption of the GATT in 1947 to the conclusion of the Uruguay Round in 1994, the members of the trade regime were able to successfully conclude eight rounds of multilateral trade negotiations, which contributed to bringing down tariff barriers on manufactured goods from an average of 40 per cent in 1947 to an average of 4 per cent in 1995, brought the particularly difficult issue of trade in agricultural goods into the realm of multilateral trade rules, and expanded the WTO's scope to include a wide array of regulatory issues traditionally confined within the boundaries of domestic governance.

With the successful conclusion of the Uruguay Round, however, the capacity of the multilateral trade regime to perform its legislative function seems to have come to a halt. In November 2001, the Doha Development Round was launched with great fanfare. It promised to bring about a broad legislated trade deal that would significantly deepen existing commitments for the reduction of barriers to trade in service, agricultural, and manufactured goods, and the protection of intellectual property rights (IPRs), as well as to further expand the WTO's regulatory reach on issues such as government procurement, trade facilitation, competition, and environmental protection. Despite these ambitions, the Bali 2013 agreement's narrow focus on trade facilitation illustrates that the Doha Round failed to produce a significant move forward in multilateral trade liberalisation. As a result of the WTO's inability in this regard, members of the multilateral trade regime have largely shifted to bilateral and regional deal making in trade diplomacy.

In short, the developments that have characterised the multilateral trade regime in the last two decades suggest that WTO lawmaking has moved out of the legislative venue of the member states and into the courtroom (Goldstein and Steinberg 2009). That is, concomitantly with judicial politics gaining centre stage in multilateral trade governance, legislative trade liberalisation in the form of negotiated multilateral trade deals has gone out of business.

Are these two processes connected in some way? The conventional wisdom posits that the causal arrow goes from the crisis of legislative lawmaking to the strengthening of judicial lawmaking. According to this view, judicial politics have become a central feature of the multilateral trade regime *because* of the failure of

multilateral trade negotiations. The increased heterogeneity of WTO members' preferences due to the rising number of member states, the politicisation of trade policymaking brought about by the inclusion of regulatory issues in the WTO's agenda, and the ability of rising economic powers, such as China, India and Brazil, to sustain a common and unified position in the Doha Round have all been considered key factors to explain the stalemate of multilateral trade deal making (De Bièvre and Poletti 2014).

While these factors have certainly been important in making bargaining in the Doha Round a more complicated business than in previous trade rounds, it is worth investigating whether, and if so to what extent, the WTO has become unable to perform its legislative function *precisely* because it has equipped itself with stronger enforcement mechanisms. In fact, the argument about the existence of systematic causal links between the creation of strengthened enforcement mechanisms and multilateral deal making in the WTO is not new. In a seminal article published a year before the Doha Round was even launched, Goldstein and Martin (2000) warned us about the potential downsides of judicial politics. They suggested that, while strengthening enforcement mechanisms could enhance the WTO's ability to bring about compliance with existing rules, it could also bring about unintended effects that interfere with the pursuit of progressive liberalisation through multilateral trade agreements.

Have the predictions of these authors been correct? Have the members of the WTO gone too far in putting in place a quasi-judicial system of rule enforcement? Addressing these questions is not only key to advancing the scholarly debate on how international institutions can foster cooperation in an anarchical system that lacks centralised enforcement; it is also crucial from a real-world perspective, particularly for the stakeholders involved in the policy debate about how global trade governance should look in the time to come. Should we expect a permanent demise in negotiated trade liberalisation at the WTO? If judicial politics indeed work as a systematic impediment on the path towards broad multilateral trade deal making, we might as well say goodbye to the system that so successfully liberalised global trade for more than half a century. In that case, we should get ready to deal with a world in which the WTO merely serves as a system that can at best incentivise compliance with existing global trade rules and accept that lawmaking will take place primarily in other fora. Most likely, then, we should come to terms with the fact that Preferential Trade Agreements (PTAs) will be the only hothouse in which tomorrow's negotiated trade liberalisation is going to take place (Mavroidis 2015). On the other hand, if one were to find that judicial politics do not necessarily make WTO members shy away from negotiated trade liberalisation, future global trade governance may turn out to be one in which new forms of negotiated trade liberalisation, such as through PTAs, can coexist with multilateral trade deals constructed under the auspices of the WTO.

This book addresses the important, and surprisingly under-researched, question of whether, and if so how, judicial politics have affected the prospects for cooperation in the WTO. Has judicialisation made WTO members more or less prone to further cooperation, either by deepening existing commitments or

Chapter Two

Judicial Politics and the Litigation-Negotiation Nexus

Few would question that international institutions have become a central feature of contemporary international relations. To a greater or lesser extent, virtually all economic, political and social activities are now subject to rules decided upon, implemented, monitored and enforced by international institutions of various sorts. Domestic institutions have, of course, not gone out of business. The bulk of the regulatory process is still carried out by actors placed within the traditional boundaries of nation states. Yet, it is beyond doubt that elements of the regulatory process have increasingly migrated to the international level. Areas as diverse as trade, finance, the environment, human rights and even national security are more and more subjected to rules developed under the auspices of international institutions (Mattli and Woods 2009).

These international institutions vary a great deal. Some international institutions have a global reach and include virtually all existing states, while others have a membership that is explicitly restricted to particular subsets of states. International institutions also vary greatly in their scope, with some focusing on single issues while others regulate multiple issue areas (Hooghe and Marks 2014). Finally, some international institutions are designed to allow for a high degree of participation by non-state actors, while participation in others is strictly restricted to public officials (Tallberg *et al*. 2014).

In addition to these important dimensions, international institutions also vary hugely in the extent to which they impose constraints on the behaviour of governments. As widely acknowledged, international governance has witnessed a steady rise of legalisation in recent years (Goldstein *et al*. 2000). In a wide array of issues areas, states have increasingly subjected themselves to binding international legal constraints. In the most institutionalised forms of legalisation precise and obligatory legal commitments are backed up by effective and credible enforcement mechanisms. International governance has thus not only witnessed a move to governance by law, but also a flourishing of international tribunals and courts with powers largely independent of the states that established them (Alter 2012; Hooghe *et al*. 2013; Posner and Yoo 2005). While the world has not moved towards a single judicial system that resembles a domestic hierarchical judiciary, some international institutions are today characterised by a high degree of judicialisation; that is, they have established precise, obligatory and binding legal commitments in combination with credible enforcement mechanisms in the form of compulsory third party adjudication to resolve disputes and foster compliance.

Is this increasing judicialisation of international institutions good news for cooperation in international relations? There are two ways to address this question. The first, and more intuitive, is to assess whether these enforcement mechanisms make compliance with the rules by the states that have established them more likely. Logic and empirical evidence suggest that the answer to this question should be affirmative. In order to understand the probability of compliance with the rules embedded in international institutions one must consider the interaction of law with the probability of enforcement (Davis 2012). The stronger the enforcement mechanisms in place, the higher the probability of strict compliance. Moreover, a host of empirical studies has shown that institutions which possess stronger enforcement mechanisms indeed tend to induce greater compliance with agreed upon rules relative to those that rely on weak enforcement mechanisms (Tallberg and McCall Smith 2014; Zangl 2008; Zangl *et al*. 2012).

A second, and perhaps more fundamental, way to address this question is to assess whether the rise of judicial politics in international relations makes states more or less willing to further their cooperative arrangements. As regime theory has long taught us, international institutions can act as mechanisms to regularise interactions and play repeated games, which often leads to an amending or expansion of the initial cooperative arrangements. To put it simply, international institutions often also perform a legislative function. It gives the states that have created them a forum for bargaining which might lead to the adoption of new rules and to a deepening and an expansion of their mutual commitments. To paraphrase a seminal article of a couple of decades ago (Downs *et al*. 1996), the question is not only whether the rise of judicial politics in international politics is good news for compliance, but also whether the good news about compliance is good news for cooperation.

The WTO is an important case for assessing how judicial politics affects the prospects of cooperation in international relations. It is the most notable example of an international political system in which a quasi-judicial system for the enforcement of rules has been put in place to integrate and back up an already existing and highly successful institutional structure for deal-making, namely the multilateral trade rounds which had been the backbone of the trade regime since the creation of the GATT. As two decades have now passed since the DSM was put into place, it is time to take stock of whether, and if so how, the strengthening of enforcement mechanisms has exerted systematic effects on the international trade regime's ability to perform its legislative function.

The political system of the multilateral trade regime

Contemporary multilateral trade relations are governed by a stable and highly institutionalised international regime, the WTO. Created in 1995 as the successor to the GATT, which had been adopted in 1947 in the aftermath of World War II, the WTO governance system can be broken down into three components: a set of rules and commitments, a negotiating forum, and an institutional location for dispute settlement. The WTO embodies a set of principles and fundamental rules

that provides the overarching legal framework under which trade relations should be carried out. While the principle of market liberalism, or the desirability of trade liberalisation, provides the underlying rationale for the entire system, the principle of non-discrimination gives market liberalism operational meaning. For an open international trading system to operate efficiently, members should not be allowed to provide special treatment to some trading partners at the expense of others. The Most Favoured Nation (MFN) and National Treatment clauses contained, respectively, in Articles 1 and 3 of the GATT translate the non-discrimination principle into binding legal commitments. The former article mandates that members of the regime automatically extend any privileges granted to individual members to all others, while the latter prohibits treating national producers more favourably than foreign ones.

Besides embodying these broad principles and rules that form the foundation of the multilateral trading system, the WTO performs two distinct functions. The institutional structure of the international trade regime has both a legislative function in the form of recurrent multilateral trade negotiations and an adjudicative function through the dispute settlement mechanism.

Since the inception of the GATT in 1947, the structure of reciprocal concessions in multilateral trade rounds has been the cornerstone of the regime. Trade rounds have for a long time essentially consisted of a series of deals aimed at lowering and eliminating tariffs to trade in industrial goods through reciprocal concessions. In the early phase of the GATT system, these reciprocal tariff reduction agreements consisted of deals struck bilaterally on a product-by-product basis (Jupille *et al*. 2013; Gowa and Kim 2005). This means that multilateral trade liberalisation in the trade regime was achieved thanks to bilateral agreements on market access that were extended to all members of the trade regime by virtue of the MFN. In the early phase of the GATT, the decision-making logic was therefore bilateral whereas the policy outcomes were multilateral (Martin 1992).

When members of the trade regime seek to coordinate their positions on general rules, particularly on matters of regulation, but also on questions of institutional design, the decision-making logic that applies is no longer bilateral but moves in the direction of multilateral consensus. As average tariff barriers to trade in manufactured goods were reduced to low levels, members of the trade regime started to realise that significant barriers to trade persisted in the form of distinct domestic regulatory practices. Hence, the international trade agenda has increasingly expanded into regulatory issues that have traditionally been within the scope of domestic institutions, and the need for multilateral consensus has, thus, become increasingly important over time. While the issue of non-tariff barriers first came onto the international trade agenda during the Tokyo Round (1973–9), it is the Uruguay Round (1986–94) that marked a real qualitative leap in the nature of cooperation in the trade regime. With the Uruguay Round and the creation of the WTO, cooperation in the trade regime forcefully moved beyond the traditional realm of negative integration by introducing positive obligations to adopt new measures in a host of different areas such as services, intellectual property rights, investments, technical standards and food safety and animal health

issues (De Bièvre 2004). This form of market integration introduced regulation in areas of public policy that had traditionally been exclusively under the scope of sovereign nation-states, and often required the reform of domestic institutional arrangements. The expansion of the trade regime's scope of action has thus meant that consensus decision-making has gradually become more important within it.

So until the launch of the Uruguay Round in 1986, GATT rounds were characterised by the separation of issues into discrete negotiations, ranging from negotiations on a product-by-product basis, to negotiations on linear tariff cuts for all products within broad sectors, to negotiations on the adoption of regulatory standards. This means that members of the trade regime were allowed to choose whether they would sign up to the various codes negotiated (Daugbjerg and Swinbank 2008; Jackson 1998; Paemen and Bensch 1995). This logic of a 'GATT à la carte', however, dramatically changed with the launch of the Uruguay Round in 1986 when members of the trade regime decided that the launching, implementation and outcome of negotiations would be treated as a 'single undertaking' in which negotiations on the different issues would be bound into a single package via the 'nothing is agreed until everything is agreed' rule (Croome 1999).

With this move, the members of the trade regime systematically introduced linkages between negotiation issues. This move was forcefully pushed for by developed trading entities such as the US and the EU in order to ensure that concessions in areas such as agriculture and textiles could be offset by the gains that they could obtain as a result of new agreements on services and intellectual property rights. To ensure the success of this issue-linkage strategy, the EU and the US issued threats of exclusion towards recalcitrant members. They required that GATT membership be cancelled before accession to the WTO, so that non-discriminatory access to their lucrative markets would only be guaranteed to states subscribing to all agreements in the Single Undertaking (Steinberg 2002). All WTO commitments that members entered into from this point were to become characterised by a very high degree of stability, as any substantial change to them would have to be decided under the same multilateral consensus decision rule and would have to be part of a new overall package deal.

The third component of the WTO's governance system is the DSM. The DSM is the enforcement mechanism that the members of the trade regime devised to address two issues: first, when members of the trade regime conclude liberalisation agreements and subsequently disagree over whether a particular trade partner is complying with the terms of such agreements; second, and ultimately the main purpose of the DSM, to incentivise compliance with any agreed rules. Non-compliance with any rules may result from a failure to implement existing rules or from the imposition of new trade barriers that happen to be inconsistent with existing rules.

The existence of a mechanism for the enforcement of agreed rules is key to overcoming the problems of cooperation that are typical in international trade relations. Indeed, any cooperative equilibrium in the form of agreements on the liberalisation of trade is bound to remain unstable as long as robust and effective

enforcement mechanisms are not put in place. States face ever-present and powerful incentives to renege on their trade liberalisation commitments, either by failing to implement the rules they have negotiated or by raising new trade barriers contravening the rules they have agreed. For instance, as long as a state has sufficient market power to affect the world prices of particular goods, it has an interest in using tariffs to improve its terms of trade while forcing the costs onto its trading partners. Also, states face powerful domestic pressures to cater to the preferences of import-competing producers that face intense competition as a result of trade liberalisation. Following on from the logic that trade represents a prisoner's dilemma, enforcement mechanisms are deemed necessary to avoid collectively sub-optimal outcomes. Indeed, cooperation on trade liberalisation is only possible as long as institutional mechanisms ensure that cheating in the form of trade protection generates greater costs than short-term benefits (Mayer 1981; Keohane 1984; Martin 1992; Staiger 1995; Bagwell and Staiger 2002). In trade agreements, the key enforcement tool is reciprocity: if you do not abide by your market opening commitments, I will respond in kind; if you do respect your commitments, so will I. It is, in other words, a simple tit-for-tat. This expectation structures bilateral interaction and actually makes trade agreements largely self-enforcing so that strictly speaking no international institution is necessary. Yet, the incentive to unilaterally misrepresent information or to abuse one's market power creates demand for the provision of reliable and more independent information about the nature of purported violations of previously agreed rules, a function that can only be reliably performed by the multilateral institution itself.

The dispute settlement mechanism of the multilateral trade regime thus helps states to commit to maintaining open markets (Davis 2012). In addition to the increased scope of trade rules, this enforcement mechanism of the multilateral trade regime has also changed significantly over time. With the creation of the WTO, members of the trade regime decided to strengthen the existing mechanism for rule enforcement by replacing the GATT's model of political–diplomatic dispute settlement with a quasi-judicial model. While the GATT did have a DSM, the ability of a defendant to block the establishment of a panel or the adoption of a ruling limited the enforcement capacity of states (Davis 2012). This does not mean that this institutional mechanism was ineffective. Dispute settlement procedures in the GATT period were activated in more than 200 cases and states generally complied with the rulings (Hudec 1993). The system was also quite effective in creating negotiated settlements during the consultation phase of the dispute settlement procedure (Busch and Reinhardt 2000, 2003). More generally, the largely bilateral commitments of the reciprocal tariff concessions of the GATT period were easily enforceable through the tit-for-tat withdrawal of concessions and thus to a large extent self-enforcing, especially between markets of approximately the same size (De Bièvre 2006a).

Yet, the largely political–diplomatic nature of this system was deemed insufficient for enforcing compliance with regulatory commitments that address barriers to trade located behind national borders. More specifically, when in 1988 the US Congress mandated that the US Trade Representative use Section 301