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Joel P. Trachtman*

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Abstract

This brief Essay summarizes, updates, and integrates work I have done elsewhere in order to suggest, first, why cost-benefit analysis is not used in dispute settlement, second, how to evaluate substitute formulae that are available for use within dispute settlement, and finally, how dispute settlement and treaty-making relate to one another in this field. This Essay considers the role of international discipline by dispute resolution bodies, in comparison to multilateral treaty-making or other legislation. Treaty-making or other legislation may take the form of harmonization to one degree or another, or importantly, may take the form of agreed rules of prescriptive jurisdiction, such as mutual recognition or national treatment.

INTERNATIONAL TRADE AS A VECTOR IN DOMESTIC REGULATORY REFORM: DISCRIMINATION, COST-BENEFIT ANALYSIS, AND NEGOTIATIONS

*Joel P. Trachtman**

INTRODUCTION

In a variety of ways, trade values conflict with other regulatory values. In fact, by its very nature, regulation is an intervention in—a conflict with—the market. If the market would achieve the desired regulatory result by itself, no regulation would be needed. Certainly regulation can *improve* the operation of markets, and in this sense regulation may be consistent with a desire for efficient markets. However, the presumptive reason for other kinds of regulation—for protective or prudential regulation—is that the market itself does not sufficiently protect the relevant values. In these specific cases, political decision-making evaluates and overrides the market. This is as it should be, and it works reasonably well in domestic systems. However, in an interstate or in an international system, the capacity to impose trade detriment on others, while enjoying the regulatory benefit at home,[1] or, even less benignly, the capacity to use regulation to achieve protectionist goals, raise additional issues.

An initial analysis would suggest that in theory, cost-benefit analysis (i) encompassing all costs and benefits including "post-material" costs, (ii) encompassing both domestic and foreign costs and benefits, and (iii) operating dynamically to seek out the unique result that maximizes net benefit (or minimizes net detriment), would be the unique best institutional structure for responding to conflicts between trade values and other regula-

* Professor of International Law and Dean *ad interim*, The Fletcher School of Law and Diplomacy, Tufts University, Medford, Massachusetts 02155. This Essay was prepared for the Organisation for Economic Co-Operation and Development ("OECD") Workshop on Regulatory Reform and the Multilateral Trading System, December 7-8, 2000. I appreciate the insights offered by other participants in that workshop.

1. *See, e.g.*, Stephen Fidler, *EU Rules 'May Cost Africa $700m'*, FIN. TIMES, Oct. 25, 2000 (citing TSUNEHIRO OTSUKI ET AL., THE WORLD BANK, SAVING TWO IN A BILLION: A CASE STUDY TO QUANTIFY THE TRADE EFFECT OF EUROPEAN FOOD SAFETY STANDARDS ON AFRICAN EXPORTS (2000)).

tory values. However, I have found no instances of this type of cost-benefit analysis being used anywhere in order to address conflicts between trade and other regulatory values.

Of course, once global cost-benefit analysis begins to include in its calculation adverse effects of regulation on foreign persons,[2] either in the form of non-pecuniary externalities or pecuniary externalities, some kinds of regulation will appear more costly. On the other hand, regulation that protects foreign persons or removes externalities will appear more beneficial. Environmentalists and deregulators alike would be required to accept the consequences of thinking globally and acting locally.

This brief Essay summarizes, updates, and integrates work I have done elsewhere in order to suggest, first, why cost-benefit analysis is not used in dispute settlement,[3] second, how to evaluate substitute formulae that are available for use within dispute settlement, and finally, how dispute settlement and treaty-making relate to one another in this field.[4] This Essay considers the role of international discipline by dispute resolution bodies, in comparison to multilateral treaty-making or other legislation. Treaty-making or other legislation may take the form of harmonization to one degree or another, or importantly, may take the form of agreed rules of prescriptive jurisdiction, such as mutual recognition or national treatment.

I. *DISPUTE RESOLUTION MECHANISMS FOR DISCIPLINING NATIONAL REGULATION*

Dispute resolution mechanisms, such as the World Trade Organization[5] ("WTO") dispute settlement system, can be given a variety of types of mandate. Tribunals may be instructed to search for discrimination (national treatment or most-favored nation treatment ("MFN")), to determine whether the national

2. As shown in a paper by the OECD Secretariat, *Trade and Regulatory Reform: Insights from the OECD Country Reviews and Other Analyses*, TD/TC/WP(2000)21/Final (Dec. 7-8, 2000), few states formally consider effects on international trade as part of their domestic regulatory review processes.

3. For an extended analysis, see Joel P. Trachtman, *Trade and . . . Problems, Cost-Benefit Analysis and Subsidiarity*, 9 EUR. J. INT'L L. 32 (1998).

4. For an extended analysis, see Joel P. Trachtman, *The Domain of WTO Dispute Resolution*, 40 HARV. INT'L L.J. 333 (1999).

5. Marrakesh Agreement Establishing the World Trade Organization, LEGAL INSTRUMENTS—RESULTS OF THE URUGUAY ROUND vol. 1, 33 I.L.M. 1144 (1994) [hereinafter WTO Agreement].

measure is a rational means to a legitimate end, to determine whether the national measure disproportionately impedes trade, or to determine whether the national measure is the least trade restrictive alternative reasonably available to achieve its end.

A. *Multilateral Rules Restricting Discrimination: National Treatment and MFN*

Since 1947, the General Agreement on Tariffs and Trade[6] ("GATT") has contained requirements of national treatment and MFN treatment in regulation. These types of requirements are viewed as less intrusive on national prerogatives than requirements of proportionality, least trade restrictive alternative requirements, balancing tests or cost-benefit analysis. However, it will be shown below that anti-discrimination norms may require a rather high degree of intrusion. On the other hand, anti-discrimination norms may fail to discipline national measures that hurt other states more than they help the state that imposes the measure.

B. *GATT Experience and the Like Products Problem*

There seems to be little objection to anti-discrimination rules, such as the national treatment obligation contained in Article III of GATT, or the MFN obligation contained in Article I of GATT. However, these provisions, as applied, involve considerable scrutiny, sometimes quite strict, of domestic regulatory measures. They do so in two ways.

In a narrower range of cases, national treatment discipline is dependent on the product-process distinction. That is, in recent cases, where a regulation is viewed as applying to a production process, as opposed to a product as such, Article III is viewed as inapplicable.[7]

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6. General Agreement on Tariffs and Trade, Oct. 30, 1947, 61 Stat. A-11, T.I.A.S. 1700, 55 U.N.T.S. 194 [hereinafter GATT].

7. *See, e.g.*, United States—Restrictions on Imports of Tuna, Mar. 23, 1993, 39 B.I.S.D. 155 (1993), *reprinted in* 30 I.L.M. 1594 (1991). For discussions of the product/process distinction, see Robert E. Hudec, *The Product-Process Doctrine in GATT/WTO Jurisprudence, in* NEW DIRECTIONS IN INTERNATIONAL ECONOMIC LAW: ESSAYS IN HONOUR OF JOHN H. JACKSON (Marco Bronckers & Reinhard Quick, eds., 2000); Robert Howse & Donald Regan, *The Product/Process Distinction-An Illusory Basis for Disciplining 'Unilateralism' in Trade Policy*, 11 EUR. J. INT'L L. 249 (2000), and the cogent response to the Howse/Regan paper from John Jackson.

More importantly, and more generally, any prohibition of discrimination requires a prior determination that two products or services are sufficiently "like" to merit equal treatment. The "like products" issue can be a proxy for a judicial examination of the rationality of regulatory categories. As in the recent *Asbestos* WTO panel decision,[8] the determination of "likeness" is often outcome determinative. WTO jurisprudence has so far declined to provide a very specific definition of "like products," but perhaps the *Asbestos* case will provide an occasion for the Appellate Body to address this issue. The panel in that case declined to consider risk as a basis for finding products to be un-"like." This position, if followed, would eviscerate the protection heretofore thought provided to good faith, non-discriminatory regulation under Article III of GATT. Of course, for most kinds of product standards, these types of measures would be subject to scrutiny under the Agreement on Technical Barriers to Trade[9] ("TBT Agreement") or under the Agreement on Sanitary and Phytosanitary Measures[10] ("SPS Agreement").

My point here is simply that issues of discrimination are not so simple as they are sometimes thought to be, and that they involve some difficult judgments. The judgment of whether two products are "like" may be made using relatively discrete factors, such as characteristics of the product, end-uses, cross-elasticity of demand, etc. However, the decision whether two products are "like" is viewed as a "case-by-case" decision, with much latitude for judgment. Rules of national treatment are not necessarily deferential to national regulation, as shown by the experience of the recent *Asbestos* case, nor are they necessarily predictable in their operation.

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8. *See European Communities—Measures Affecting Asbestos and Asbestos-Containing Products*, Report of the Panel, WT/DS135/R, paras. 8.130-.132 (Sept. 18, 2000) (holding that risk to health is not a factor in determining "likeness" under article III of GATT); *see also United States—Measures Affecting Alcoholic and Malt Beverages*, DS23/14 (noting that "the treatment of imported and domestic products as like products under Article III may have significant implications for the scope of obligations under the General Agreement and for the regulatory autonomy of contracting parties").

9. Agreement on Technical Barriers to Trade, Apr. 15, 1994, WTO Agreement, Annex 1A, *at* http://www.wto.org/english/docs_e/legal_e/final_e.htm.

10. Agreement on Sanitary and Phytosanitary Measures, Apr. 15, 1994, WTO Agreement, Annex 1A, *at* http://www.wto.org/english/docs_e/legal_e/final_e.htm.

II. *THE PROBLEMS OF COST-BENEFIT ANALYSIS AND THE ALTERNATIVES*

As noted above, in economic theory, at least on an initial examination, courts would be given a mandate to engage in all-inclusive, dynamic, cost-benefit analysis in order to decide questions of conflict between local regulation and global trade. Assuming that courts could perform this cost-benefit analysis accurately, this would be the first-best solution to the trade versus domestic regulation issue. (Note that *international* regulation does not raise the same kinds of issues). But such cost-benefit analysis is not explicitly used anywhere. Instead, courts receive mandates to apply the following types of tests, individually or in combination, and with many subtle differences within each type of test:

1. *National treatment rules.* A national treatment rule is a type of anti-discrimination rule that examines whether different legal standards are applied to comparable cases, as between the domestic and the foreign.
2. *Simple means-ends rationality tests.* These tests consider whether the means chosen is indeed a rational means to a purported end. Analytically, simple means-ends rationality testing is included in all of the tests described below in this list, and is sometimes used as a proxy to detect discrimination. As it imposes little real discipline, and is often included in other tests, I do not analyze the use of simple means-ends rationality testing in detail below.
3. *Necessity or least trade-restrictive alternative tests.* This type of test inquires whether there is a less trade restrictive means to accomplish the same end. The definition of the end is often outcome-determinative. In some cases necessity testing is qualified by requiring that the means be the least trade restrictive alternative that is *reasonably available.* In addition, necessity testing is sometimes combined with limitations on the categories of ends permitted.
4. *Proportionality.* Proportionality *stricto sensu*[11] inquires whether the means are "proportionate" to the ends:

11. NICHOLAS EMILIOU, THE PRINCIPLE OF PROPORTIONALITY IN EUROPEAN LAW: A COMPARATIVE STUDY 6 (1996). A wider definition of proportionality developed in the EU context includes three tests: (i) proportionality *stricto sensu,* (ii) a least trade restric-

whether the costs are excessive in relation to the benefits. It might be viewed as cost-benefit analysis with a margin of appreciation, as it does not require that the costs be less than the benefits. Proportionality may be either static or comparative, in the same way as cost-benefit analysis. A comparative approach to proportionality testing would include in its calculus the costs and benefits of alternative rules.

5. *Balancing Tests.* Balancing tests purport to decide whether a measure that impedes trade is acceptable, balancing all of the factors. Balancing may be viewed as a kind of amorphous or imprecise cost-benefit analysis.[12] More charitably, and perhaps more correctly, it may be viewed as a kind of cost-benefit analysis that recognizes the difficulty of formalizing the analysis, and seeks to achieve similar results informally.[13]
6. *Cost-benefit analysis.* Static cost-benefit analysis in the context at hand[14] juxtaposes the regulatory benefits of regulation with the trade costs of regulation, as well as other costs of regulation, and would strike down regulation where the costs exceed the benefits. Cost-benefit analysis in this context may be viewed as stricter scrutiny than the

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tive alternative test, and (iii) a simple means-ends rationality test. This Essay will consider only the narrower type of proportionality.

12. *See* Michael E. Smith, *State Discriminations Against Interstate Commerce*, 74 CAL. L. REV. 1203, 1205 (1979) (stating that "the Justices take all relevant circumstances into account and render judgment according to their overall sense of the advantages and disadvantages of upholding the regulation"). At their most precise, balancing tests are the same as cost-benefit analysis. *See* Earl M. Maltz, *How Much Regulation is Too Much—An Examination of Commerce Clause Jurisprudence*, 50 GEO. WASH. L. REV. 47, 59-60 (1981).

13. "If we had a way of quantifying all the appropriate inputs, and a way of comparing them, and a theory that told us how to do so, we would not call it balancing. Rather, it would be called something like 'deriving the most cost-effective solution,' or just 'solving the problem.'" Stephen E. Gottlieb, *The Paradox of Balancing Significant Interests*, 45 HASTINGS L.J. 825, 839 (1994). *See also* T. Alexander Aleinikoff, *Constitutional Law in the Age of Balancing*, 96 YALE L.J. 943, 1002-1004 (1987).

14. For more general and technical treatment of cost-benefit analysis, see, e.g., PETER S. MENELL & RICHARD B. STEWART, ENVIRONMENTAL LAW AND POLICY 81-160 (1994); D. PEARCE & C. NASH, THE SOCIAL APPRAISAL OF PROJECTS: A TEXT IN COST-BENEFIT ANALYSIS (1981); R. Tresch, Public Finance: A Normative Theory (1981); EDITH STOKEY & RICHARD ZECKHAUSER, A PRIMER FOR POLICY ANALYSIS (1978); E.J. MISHAN, COST-BENEFIT ANALYSIS (1976); H. RAIFFA, DECISION ANALYSIS (1968). *See also* the recent special issue of The Journal of Legal Studies devoted to cost-benefit analysis, beginning at 29 J. LEG. STUDS. 837 (2000) (including papers by W. Kip Viscusi, Amartya Sen, Martha Nussbaum, Richard Posner, and Gary Becker).

> U.S. domestic cost-benefit analysis that has recently become popular, as it adds a cost dimension not normally included: detriments to trade. Adding trade detriments to the calculation would presumably have the marginal effect of causing some regulation to fail a cost-benefit analysis test. It is worth comparing static cost-benefit analysis, simply juxtaposing the costs and benefits of a single rule, with a more dynamic comparative cost-benefit analysis, comparing the net benefits of multiple rules, and recommending the rule with the greatest net benefits.

There are several reasons why a full cost-benefit analysis test may indeed be less than optimal, and one or more of these other tests might be preferred. In this Essay, I evaluate some of the parameters by which cost-benefit analysis might be compared with other tradeoff devices: (i) maximization of net gains of trade and regulation, (ii) administrability, (iii) distributive concerns, (iv) moral concerns, and (v) theoretical concerns. These factors are not themselves commensurable, and so we cannot place them on a simple tote board to determine when comparative cost-benefit analysis should or should not be used. Rather, these factors must be examined and subjected to political or deliberative analysis in order to determine which tradeoff device should be used in particular circumstances.

However, very briefly,[15] it is clear that cost-benefit analysis experiences severe problems of administrability (including predictability). Cost-benefit analysis does not concern itself with the distribution of the costs and benefits, and so it could raise significant distributive issues. Cost-benefit analysis raises important moral concerns regarding the commensurability between different kinds of values, including especially between material and post-material values. Political institutions, as opposed to adjudicative or research institutions, are most appropriate to commensurate among these types of values. Cost-benefit analysis raises related theoretical concerns in economics about its implicit interpersonal comparison of utility: your valuation of the environment cannot be compared by a third party to my valuation of an SUV.

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15. For a more extended analysis, see Trachtman, *supra* note 3.

My analysis suggests that a least trade restrictive alternative analysis overcomes some of the most difficult of these concerns, and might be worthy of consideration. First, as it only measures the detriment to trade, not the benefits of regulation, it is easier to administer. Second, it does not seek to commensurate between these values, as it simply seeks the method of satisfying the non-trade values that imposes the least detriment in trade terms. For similar reasons, it raises fewer concerns regarding interpersonal comparison of utility.

Let us be clear, though, that least trade restrictive alternative analysis might leave in place a domestic regulation that provides benefits far smaller than the trade detriments it causes, and might strike down domestic regulation that is far more valuable than the trade detriments it causes. Thus, it is both under-inclusive and over-broad. Of course, least trade restrictive alternative analysis has been adopted judicially in connection with the application in some circumstances of Article XX of GATT, and has been adopted "legislatively" in both the SPS Agreement[16] and the TBT Agreement.[17]

A. *"Legislative" versus Judicial Decision-Making and Rules versus Standards*

While trade diplomats and scholars have expressed pride at the Uruguay Round achievement of more binding and more "law-oriented" dispute resolution, the same group and a variety of non-governmental organizations ("NGOs") and other commentators question the jurisdictional scope of dispute resolution. After all, should these small tribunals, lacking direct democratic legitimacy, determine profound issues confronting the international trading community, such as the relationship between trade values and environmental values? Many voices have called for greater international legislation (specific treaty-making) in these important fields. This section is intended to outline a more realistic and nuanced view, based on law and economics analytical techniques. It is intended to suggest the reasons why dispute resolution could be the appropriate place to determine

16. *See* Agreement on the Application of Sanitary and Phytosanitary Measures, Apr. 15, 1994, WTO Agreement, Annex 1A, arts. 2.2, 5.6, *at* http://www.wto.org/english/docs_e/legal_e/final_e.htm.

17. *See* Agreement on Technical Barriers to Trade, Apr. 15, 1994, WTO Agreement, Annex 1A, art. 2.2, *at* http://www.wto.org/english/docs_e/legal_e/final_e.htm.

these issues. Conversely, it is intended to suggest a way to determine or predict when these issues might better be subjected to more specific legislative action.

The analysis above of different "tradeoff devices" assumes that a legislative act (including the entry into a treaty) has assigned a mandate to a court. However, in addition to a choice among mandates to courts, there is a choice *whether and to what extent* to provide a mandate to courts. It is possible for the legislative act to provide either a broad or a narrow mandate to a court. A narrow mandate will call for less discretion to be exercised by the court. Economic analysis provides two related analytical techniques that suggest when the authors of treaties might decide to accord narrower or broader mandates to courts.

Not only do treaty-writers delegate authority to dispute resolution tribunals, they also maintain complex relationships with the dispute resolution process, both formal and informal. First, of course, is the possibility of legislative reversal: if the authors of the treaty become discontented with the manner of its application, they may change the treaty. Furthermore, they may restrain dispute resolution. Second, and relatively unusual in general international law, is a formal "political filter" device. This political filter was much more important prior to the 1994 changes to WTO dispute resolution, but still exists in attenuated form.

The incomplete contracts literature considers the reasons for, and implications of, the fact that all contracts (like all treaties) are necessarily incomplete in their capacity to specify the norms that will be applied to particular conduct. In the rules versus standards literature,[18] a law is a "rule" *to the extent that* it is specified in advance of the conduct to which it is applied. A standard, on the other hand, is a law that is farther toward the other end of the spectrum, in relative terms. It establishes general guidance to both the person governed and the person charged with applying the law, but does not specify in detail, in

18. For an introduction to the rules versus standards discussion in law and economics, see Louis Kaplow, *General Characteristics of Rules*, *in* ENCYCLOPEDIA OF LAW AND ECONOMICS (B. Bouckaert & G. De Geest eds., 1998); Louis Kaplow, *Rules Versus Standards: An Economic Analysis*, 42 DUKE L.J. 557 (1992); *see also*, Cass R. Sunstein, *Problems with Rules*, 83 CAL. L. REV. 955 (1995). In international trade law, "standards" has a specific meaning, referring to product standards. This meaning is separate from the sense in which "standards" is used here.

advance, the conduct required or proscribed. The relativity of these definitions is critical. Furthermore, each law is comprised of a combination of rules and standards. However, it will be useful to speak here generally of rules as separate from standards.

It is worth noting that the distinction between a rule and a standard is not necessarily grammatical or determined by the number of words used to express the norm; rather, the distinction relates to how much work remains to be done to determine the applicability of the norm to a particular circumstance.

Professor Hadfield applies an incomplete contracts analysis to statutes, which we in turn can apply to treaties.[19] Treaties may be optimally incomplete with appropriate instructions to decision-makers to complete the "contract" in particular cases. The parameters to consider include (i) the costs of advance specification, (ii) the degree to which the future is unpredictable or stochastic, (iii) the ability to customize to particular facts in specific cases, and (iv) the potential value of diversity of compliance techniques. This literature tends to treat the legislature as a unitary actor. It will be exceedingly important for us to recognize that the legislature in our case (as in Hadfield's) is a group of actors subject to strategic and social choice limitations on their ability to act.

Incompleteness of specification may not simply be a result of conservation of resources. It may be a more explicit political decision to either agree to disagree for the moment, to avoid the political price that may arise from immediate hard decisions, or to cloak the hard decisions in the false inevitability of judicial interpretation. It is important, also, to recognize that the incompleteness of specification may represent a failure to decide how the policy expressed relates to other policies. This is critical in the trade area, where often the incompleteness of a trade rule relates to its failure to address, or incorporate, non-trade policies. Thus, for example, the *chapeau* of Article XX of GATT may be viewed as providing a standard as to "arbitrariness," "justifiability," and "discrimination."

Obviously, each law is comprised of a combination of rules

19. *See* Gillian K. Hadfield, *Weighing the Value of Vagueness: An Economic Perspective on Precision in the Law*, 82 CAL. L. REV. 541, 547 (1994); *see also* Ian Ayres & Robert Gertner, *Strategic Contractual Inefficiency and the Optimal Choice of Legal Rules*, 101 YALE L. J. 729 (1992).

and standards. However, it will be useful to speak here generally of rules as separate from standards.

1. The Costs and Benefits of Rules and Standards

Rules are more expensive to develop than standards, *ex ante*, because rules entail specification costs, including drafting costs and negotiation costs, as well as the strategic costs involved in *ex ante* specification. In order to reach agreement on specification—in order to legislate specifically—there may be greater costs in public choice terms.[20] This is particularly interesting in the trade context, where treaty-making would be subjected to intense domestic scrutiny, while application of a standard by a dispute resolution process might be subjected to reduced scrutiny. On the other hand, NGOs have sought in this connection to enhance transparency in dispute resolution. Finally, rules require clear decision; standards may serve as an agreement to disagree, or may help to mask or mystify a decision made.[21] Under standards, both sides in the legislative process may claim victory, at least initially.

Rules are generally thought to provide greater predictability. There are two moments at which to consider predictability. First, is the ability of persons subject to the law to be able to plan and conform their conduct *ex ante*, sometimes known as "primary predictability."[22] The second moment in which predictability is important is *ex post*, after the relevant conduct has taken place. Where the parties can predict the outcome of dispute resolution—where they can predict the tribunal's determination of their respective rights and duties—they will spend less money on litigation. This type of predictability is "secondary predictability." Both types of predictability can reduce costs. While rules appear to provide primary and secondary predictability, tribunals may construct exceptions in order to do what is, by their lights, substantial justice, and thereby reduce predictability. It

20. *See* Gillian K. Hadfield, *Weighing the Value of Vagueness: An Economic Perspective on Precision in the Law*, 82 CAL. L. REV. 541, 550 (1994) (citing Linda R. Cohen & Roger G. Noll, *How to Vote, Whether to Vote: Strategies for Voting and Abstaining on Congressional Role Calls*, 13 POL. BEHAV. 97 (1991)).

21. Kenneth W. Abbott & Duncan Snidal, *Why States Act Through Formal International Organizations*, 42 J. CONFLICT RESOL. 3 (1998).

22. For this use of the terms "primary predictability" and "secondary predictability," see William F. Baxter, *Choice of Law and the Federal System*, 16 STAN. L. REV. 1, 3 (1963).

may be difficult to constrain the ability of tribunals to do this. Furthermore, as noted below, game theory predicts that some degree of uncertainty—of unpredictability—may enhance the ability of the parties to bargain to a lower cost solution. Thus, simple predictability is not the only measure of a legal norm; rather, we must also be concerned with the ability of the legal norm to provide satisfactory outcomes. In economic terms, we must be concerned with the allocative efficiency of the outcome. We consider allocative efficiency below as we consider the institutional dimension of rules and standards.

As we consider the relative allocative efficiency of potential outcomes, we must recognize that there is a temporal distinction between rules and standards. Standards may be used earlier in the development of a field of law before sufficient experience to form a basis for more complete specification is acquired. In many areas of law, courts develop a jurisprudence that forms the basis for codification—or even rejection—by legislatures. With this in mind, legislatures (or adjudicators) may set standards at an early point in time, and determine to establish rules at a later point in time.[23] It is clear that a rule of *stare decisis* is not necessary to the development of a body of jurisprudence by a court or dispute resolution tribunal.[24] It is also worth noting that in a common law setting, or any setting where tribunals refer to precedents, the tribunal may announce a standard in a particular case, and then elaborate that standard in subsequent cases until it has built a structure of rules for its own application.

Kaplow points out that where instances of the relevant behavior are more frequent, economies of scale will indicate that rules become relatively more efficient. For circumstances that arise only infrequently, it is more difficult to justify promulgation of specific rules. In addition, rules provide compliance benefits: they are cheaper to obey, because the cost of determining the required behavior is lower. Rules are also cheaper to apply by a court: the court must only determine the facts and compare them to the rule.

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23. *See* Kaplow, *The General Characteristics of Rules*, *supra* note 14, at 10.

24. David Palmeter & Petros C. Mavroidis, *The WTO Legal System: Sources of Law*, 92 AM. J. INT'L L. 398 (1998).

2. The Institutional Dimension of Rules and Standards

Another distinction between rules and standards, often deemphasized in this literature, is the institutional distinction: with rules, the legislature often "makes" the decision, while with standards, the adjudicator determines the application of the standard, thereby "making" the decision. Again, it is obvious that these terms are used in a relative sense (this caveat will not be repeated). Economists and even lawyer-economists seem to assume that the tribunal simply "finds" the law, and does not make it. Of course, courts can make rules pursuant to statutory or constitutional authority: the hallmark of a rule is that it is specified *ex ante*, not that it is specified by a legislature. However, at least in the international trade system, rules are largely made by treaty, and standards are largely applied by tribunals.

But the difference between legislators and courts is an important one, and may affect the outcome.[25] The choice of legislators or courts to make particular decisions should be made using cost-benefit analysis. Such a cost-benefit analysis would include, as a critical factor, the degree of representativeness of constituents: which institution will most accurately reflect citizens' desires? There are good reasons why such cost-benefit analysis does not always select legislatures. First, there is a public choice critique of legislatures. Second, even under a public interest analysis, legislatures may not be efficient at specifying *ex ante* all of the details of treatment of particular cases. Third, the rate of change of circumstances over time may favor the ability of courts to adjust. Finally, we must analyze the strategic relationship between legislators and courts. Thus, in order fully to understand the relationship between rules and standards, the tools of public choice or positive political theory[26] should be brought to bear to analyze the relationship between legislative and judicial decision-making.[27]

3. The Strategic Dimension of Rules and Standards

It is not possible to consider the costs and benefits of rules

25. *See* NEIL KOMESAR, IMPERFECT ALTERNATIVES (1994).

26. *See, e.g.*, John Ferejohn & Barry Weingast, *A Positive Theory of Statutory Interpretation*, 12 INT'L REV. L. & ECON. 263 (1992).

27. Robert Cooter & Josef Drexl, *The Logic of Power in the Emerging European Constitution: Game Theory and the Division of Powers*, 14 INT'L REV. L. & ECON. 307 (1994).

and standards separately from the strategic considerations that would cause states to select a rule as opposed to a standard. Johnston analyzes rules and standards from a strategic perspective, finding that, under a standard, bargaining may yield immediate efficient agreement, whereas under a rule, this condition may not obtain.[28] Johnston considers a rule a "definite, ex ante entitlement" and a standard a "contingent, ex post entitlement." Like Kaplow, he does not consider the source of the rule, whether legislature or tribunal.

Johnston notes the "standard supposition in the law and economics literature . . . that private bargaining between [two parties] over the allocation of [a] legal entitlement is most likely to be efficient if the entitlement is clearly defined and assigned ex ante according to a rule, rather than made contingent upon a judge's ex post balancing of relative value and harm."[29] Johnston suggests this supposition may be incorrect,[30] "When the parties bargain over the entitlement when there is private information about value and harm, bargaining may be more efficient under a blurry balancing test than under a certain rule."[31] This is because under a certain rule, the holder of the entitlement will have incentives to "hold out" and decline to provide information about the value to him of the entitlement. Under a standard, where presumably it cannot be known with certainty *ex ante* who owns the entitlement, the person not possessing the entitlement may credibly threaten to take it, providing incentives for the other person to bargain. Johnston points out that this result is obtained only when the *ex post* balancing test is imperfect, because if the balancing were perfect, the threat would not be credible. This provides a counter-intuitive argument for inaccuracy of the application of standards.[32] Interestingly, further research as to the magnitude of strategic costs under rules and under standards might suggest that over time, rules provide some of the strategic benefits of standards. This might be so if

28. Jason Scott Johnston, *Bargaining under Rules versus Standards*, 11 J. L. ECON. & ORG. 256 (1995).

29. *Id.*

30. *See also* Carol Rose, *Crystals and Mud in Property Law*, 40 STAN. L. REV. 577 (1988); Joel P. Trachtman, *Externalities and Extraterritoriality*, *in* ECONOMIC DIMENSIONS IN INTERNATIONAL LAW (Jagdeep Bhandari & Alan O. Sykes eds., 1998).

31. Johnston, *supra* note 24, at 257.

32. *Id.* at 272.

tribunals develop exceptions to rules in a way that introduces uncertainty to their application. This increased benefit would of course be countervailed to some extent by the reduction of predictability that the development of exceptions would entail.

I do not, in this brief Essay, give examples of how these considerations might apply to actual cases.[33]

B. *Improving "Legislation"*

There are several problems with the international treaty system: with international legislation. First, it is functionally Balkanized: trade, environment, health, competition, tax, etc., are all dealt with separately, and there is insufficient coordination. Second, legislation takes place largely through new treaty-making, and this generally requires unanimity. Thus, international legislation is slow to respond to many emerging, overlapping issues. By default, many of these issues are referred to dispute resolution in the WTO. The WTO dispute resolution system seems to bear too much responsibility, compared to the international legislative system. This section considers how the legislative capacity of the international regulatory system can be improved.

1. Improving Functional Integration Through Horizontal Institutional Coordination

There is already much cooperation between the WTO and the United Nations Environmental Program ("UNEP") and Multilateral Environmental Agreements ("MEAs"). There needs to be more cooperation, and at some level, the relationship between trade norms and other norms need to be worked out more definitively, and more formally. For example, the European Union has recently argued that greater clarification of the validity of MEA norms within the WTO legal system would be useful, while the United States has argued that the WTO dispute resolution system has set forth an adequate test for the validity of MEA norms that may conflict with trade norms. Functional integration could take the form of choice of law and/or choice of forum rules, when these norms come into conflict, rules regarding supremacy of norms, later in time rules, interpretative rules

33. *See* Trachtman, *supra* note 4.

that seek to avoid conflict, or at the extreme, joint formulation of norms, as we would expect within a domestic system. For example, a type of "choice of law" rule might specify that certain MEAs override certain trade law obligations.

2. Request-Offer Negotiations Regarding National Regulation

How would more specific international law regarding domestic regulation be made; how would rules regarding the interplay between trade and other norms be legislated? There may also be room for further elaboration of standards in certain areas.[34] Rules can be developed by courts through the application of standards over time. Rules are more often made by legislatures. Sometimes judicial action can act as a pathfinder for legislation: legislative action can respond, positively or negatively, to judicial action.

Thus, the United States, having lost in the *Shrimp-Turtle*[35] case, might seek new treaty action, either within or without the WTO, to approve its action. Now that the Appellate Body has spoken in that case, the onus is on the United States to seek "legislative reversal." However, the Appellate Body has not provided an extremely clear response: this is why the EU is seeking greater legislative clarification. In accordance with the strategic rules-standards perspective, the lack of perfect clarity promotes negotiation. This is an example of the problem of "asset ownership" in this field: if it were clear that WTO law never permits process standards as barriers to import, it would be for those states that wish to impose such barriers to negotiate for exceptions. Given some ambiguity, both sides have some incentive to negotiate. Negotiations take place in the shadow of judicial action.

It is important to recognize that there is a distributive aspect to these norms. In order to achieve greater specificity—in order to legislate rules—it will be necessary to negotiate transactions between states. The original WTO style of tariff negotiations—request/offer—may be appropriate for use in the regulatory field. That is, states could request exceptions for their regula-

34. On December 24, 1998, the WTO Committee on Trade in Services adopted the *Disciplines on Domestic Regulation in the Accountancy Sector*, S/L/64, developed by the WTO Working Party on Professional Services.

35. *United States—Import Prohibitions of Certain Shrimp and Shrimp Products*, Report of the Appellate Body, WT/DS58/AB/R (Oct. 12, 1998).

tion, or alternatively, states could request liberalization of another state's regulation, in exchange for another concession. The advantage of this type of transaction—a rule-based transaction—is that states would know in advance what types of modifications of their domestic regulation would be required, or what kinds of liberalization in other states they had achieved. These modifications could then be legitimated as part of the trade negotiations, instead of being left to the dispute resolution process.

Negotiations in the WTO context may provide an advantage over negotiations in a MEA or UNEP, or other functional international organization, context: the greater possibility of linked package deals. While linkages may be made across functional organizations, it is easier to do so, both administratively and in terms of legitimation, within a single organization. The WTO already contains much scope for package deals. Thus, there is a network externality argument for inclusion of additional subject matter in the WTO.

3. High-Powered Incentives to Negotiate: Selective (and Weighted?) Majority Voting as a Means to Redress the Adjudication/Legislation Imbalance

In order to provide even stronger incentives to negotiate than those existing with simply a judicial prod, states could agree on selective, and possibly weighted, majority voting. The incoming Director-General of the WTO, Thai Trade Minister Supachai, has already broached this issue. For an example of selective majority voting, states could agree that MEAs, perhaps with a specified minimum number of parties, might in the future be exempted from WTO prohibitions by majority vote. If majority voting were the applicable legislative rule, states would have greater incentives to come to terms on unanimously agreed resolution of trade versus regulation problems. Furthermore, majority voting would redress the current imbalance in the capacity to act between WTO adjudication and multilateral treaty-making.[36]

36. For a story of a similar imbalance in the European Union context, see Joseph Weiler, *The Transformation of Europe*, 100 YALE L. J. 2403 (1991).

4. Reducing the Problem of Private Information: The Potential Role of International Organizations in Evaluating Regulatory Barriers

One of the most serious obstacles to negotiations regarding regulatory barriers to trade is lack of knowledge. This ignorance exists on several dimensions: (i) what are the trade costs associated with the relevant regulation; (ii) what are the full regulatory benefits associated with the relevant regulation; (iii) is there a less trade restrictive alternative? An independent party may assist negotiations by serving as an independent source of this information, overcoming information asymmetries between the parties. Private information may impede negotiation toward the reduction of barriers.

5. Legitimating Adjudication

As indicated above, trade versus regulation decisions put a good deal of pressure on the adjudicator. Mandates that do so explicitly would help to legitimate this allocation of responsibility, while alleviating some of the criticism of the dispute settlement process. In addition, as noted above, a more effective structure for legislation would reduce concern about the legitimacy of adjudication. If legislative reversal were more readily available, adjudication would be more responsive.

CONCLUSION

Current arrangements for addressing the interface between trade and domestic regulation may not be satisfactory. National treatment standards may not be as unintrusive as advertised, and may leave in place measures that should be disciplined. Decisions to assign responsibility for disciplining national regulation must consider various alternative mandates. However, these decisions must be examined in comparison to decisions to provide greater treaty or legislative guidance. This Essay considers the choice among general standards that can form the basis for a mandate to dispute resolution bodies in juxtaposition to the choice to provide more specific treaty rules.