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by

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The Transformation of European Trading States

RICHARD H. STEINBERG

MANY HAVE CLAIMED that trade liberalization is weakening the state (Kindleberger 1971; Vernon 1971; Mathews 1997; Alesina and Spolaore 1997). Yet the state is not obviously weakening; it is transforming (Kahler and Lake 2003), as it has been doing throughout modernity (Tilly 1975; Bendix 1978; Skocpol 1979).

This chapter argues that much of the substance and process of contemporary state transformation is driven not by trade liberalization in the abstract but by the particular institutional form of trade liberalization since 1948. At the international level, the “self-regulating market” is not really “self-regulating” (Polanyi 1944). Contemporary trade liberalization has been a product of US (and, later, US-European) power, exercised through the creation and operation of the General Agreement on Tariffs and Trade (GATT) and its successor, the World Trade Organization (WTO), and reflected in the GATT/WTO’s substantive rules. The particular form and processes of trade liberalization have entailed not just the abandonment of certain national policies but also shifts of authority within the state, the creation of new kinds of state capacities, and new processes of policymaking.

European state transformation is part of this story. It is generally accepted that European Community (EC) and European Union (EU)¹ institutions have strengthened at the expense of the member states. Intergovernmental theorists explain this development as a result of

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state-driven interactions, by which the member states agreed at crucial transformative moments (such as conclusion of the Treaty of Rome, the Single European Act, and the Maastricht Treaty) to enhance the economic efficiency or competitiveness of Europe (Hoffmann 1966; Moravcsik 1998). In contrast, neofunctionalists argue that transnational public and private elites have shifted authority from the member states to Brussels for particularistic purposes (E. Haas 1958; Burley and Mattli 1993; Sandholtz and Stone-Sweet 1998). Leadership theorists focus instead on the role of informal politics and the political vision of those who have held the post of Commission president in explaining the Commission's growing role at the expense of the member states (Middlemas 1995; Loth, Wallace, and Wessels 1998; Drake 2000).

The changing organization of Western European states and EU institutions can be more fully understood by considering the exigencies of international engagement, particularly the demands of partnering with the United States to govern the institutions of the global trading system. Effective management of the GATT/WTO system has demanded the transformation of European state institutional authority, capacity, and policymaking processes relating to trade. The United States and the EU have effectively governed the GATT/WTO system since around 1970 and began more actively driving outcomes at the end of the cold war. For the EU to join the United States as a hegemonic duopolist at the GATT/WTO required changes in the organization of the European state: shifting authority upward within states and to the Commission, expanding state capacity within states and at the European level, and changing processes of member state and European trade policymaking. The desirability of playing a leadership role in GATT/WTO governance and other demands for the EC's international engagement (such as enlargement and bilateral trade conflict and cooperation) combined to favor transformation of European states. Europe chose to transform along lines that have enabled it to more effectively cooperate and compete in international trade relations and to co-govern the world trading system.

Section 1 traces and explains the shift from US hegemonic governance of the GATT system to European-US cogovernance of the GATT/WTO system. Section 2 describes and explains the transformation of European state institutional structures that enabled the EU

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to join the United States in governing the GATT/WTO system. Section 3 explains how European-US governance of the world trading system has favored changes in the organization of the state in many third countries toward a Western industrialized model of the state. The chapter concludes with speculation about the political and institutional limits on continued transatlantic governance of the global trading system.

1. Governance of the Trade Regime: From US Hegemony to Shared Transatlantic Governance

Since its establishment in 1948, the GATT/WTO system has defined the rules and principles that have shaped global trade. By virtue of its enormous market power, the United States set the rules of the system in its early years (1947–1972). The EC was a relatively small market at the time, and it had not yet established its institutional authority, capacity, and internal policymaking processes to co-govern the GATT. Starting in the early 1970s (1973–1989), the United States began sharing power over the development of GATT rules with the EC. By 1973, the EC had both the market power and institutional authority and capacity to help govern the GATT system, but the transatlantic powers were constrained in the exercise of their power by cold war competition with the Soviet Union. With the end of the cold war (1990–present), the EU and the United States have actively cooperated to advance an agenda at the GATT/WTO that reflects their similar interests. The basis of transatlantic power at the GATT/WTO will be discussed first, followed by an analysis of governance in each of the three periods outlined above.

Power at the GATT/WTO

States and customs territories, and no other entities, have legal standing in the GATT/WTO.² International institutions are voluntary organizations; states adhere to their mandates out of self-interest. Given a world of sovereign nation-states, decision-making processes either will formally reflect the interests of powerful states or will be supplemented by informal action that allows their expression of power (Krasner 1982).

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Operationalizing state “power” poses a central challenge to this line of argument. While there is some consensus that power should be defined as the ability to get others to do what they otherwise would not do, measurement is another problem (Keohane and Nye 1977). Some analysts evaluate state power in the aggregate, considering total military and economic might in order to classify countries as “great powers” or not (Waltz 1979; Gilpin 1981). But in a specific negotiating context, like trade negotiations, in which only some dimensions of power are likely to be brought to bear, the measure of power must be more narrowly tailored.

In analyzing trade relationships, market size—the capacity to open or close a market—may offer the best first approximation of bargaining power (Steinberg 2002). Most political scientists and trade economists agree that governments treat foreign market opening and associated increases in export opportunities as a domestic political benefit and domestic market opening as a cost. Hence, for example, the greater the export opportunities that can be attained, the greater the domestic political benefit to the government of the country attaining them. Market opening and closure have been treated as the currency of trade negotiations in the postwar era (Hirschman 1945; Waltz 1970; Krasner 1976). Whether trade bargaining takes the form of mutual promises of market opening, threats of market closure, or a combination of both, larger, developed markets are better endowed than smaller markets in trade negotiations. The proportionate domestic economic and political impact of a given absolute change in trade access varies inversely with the size of a national economy. An additional value of exports offers proportionately more welfare and net employment gain to smaller countries than larger ones. The political implication is that a given volume of liberalization offers proportionately less domestic political benefit to the government delivering it in the larger country. Conversely, in negotiations entailing threats of trade closure, a threat of losing a given volume of exports is a relatively less potent tactic when used against a large country than when used against a small one. Hence, it is well established that developed economies with big markets have great power in an open trading system by virtue of variance in the relative opportunity costs of closure for trading partners (Krasner 1976).

By this measure, over the course of GATT/WTO history, the

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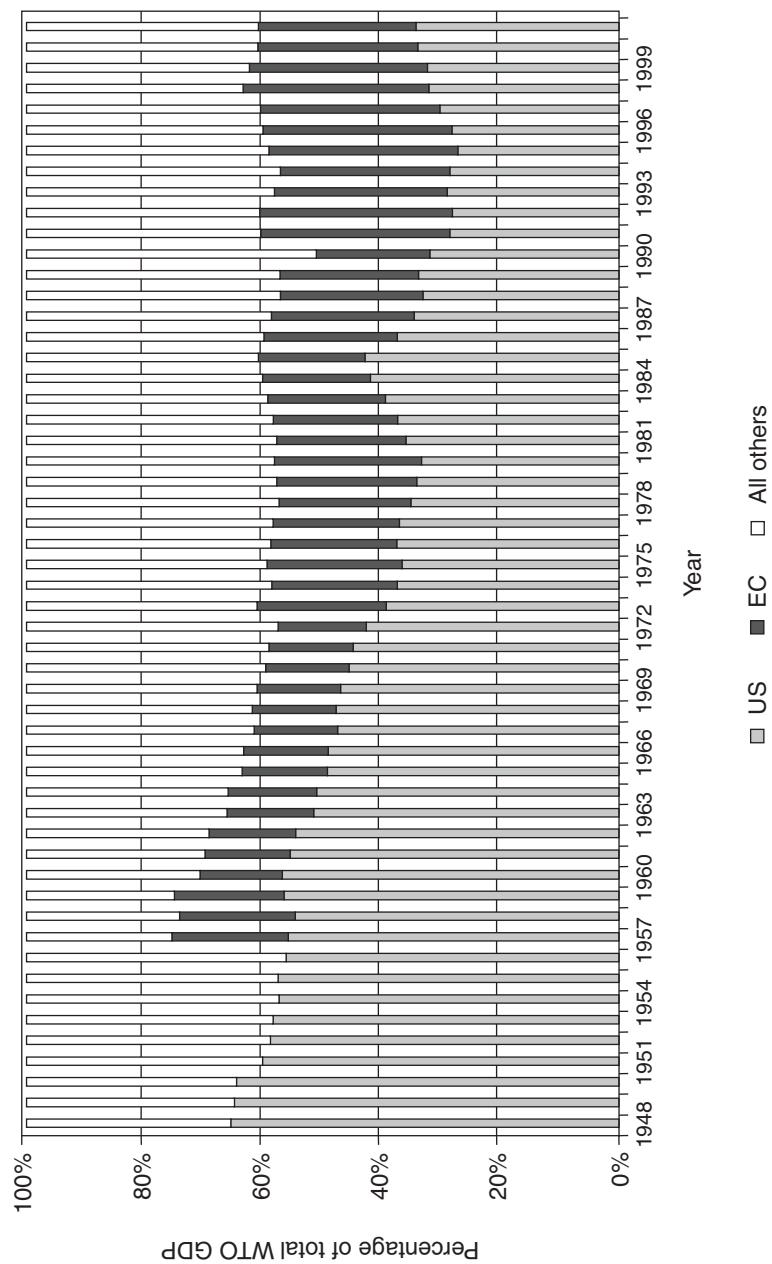


Figure 9.1 US, EC, and all other GATT/WTO shares in total WTO GDP.

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United States must be considered the dominant state in shaping GATT and WTO institutions. However, its role has waned, and increasingly it has needed to cooperate with the EU in order to govern the system. While the United States may be hegemonic on security matters, it now shares power with the EU on trade.

Figure 9.1 shows the proportion of gross domestic product (GDP) of GATT/WTO members accounted for by the United States and the EU, respectively, from 1947 to 2001. While such figures are only a best first approximation of power in the trading system (e.g., they do not account for the effects of the fall of the Soviet Union or the increased size and diversity of GATT/WTO membership), the chart illustrates the relative loss of US market power in the GATT/WTO since 1947—and the rise of Europe. In 1948, the first year the GATT was in force, US GDP accounted for about 65 percent of the total GDP of all GATT members, and combined US-UK GDP accounted for about 75 percent of the total.³ By 1970, US GDP share of the GATT total had fallen to 46 percent, and the EC share was 14 percent.⁴ By the 1990s, the US share had continued to fall, while the EC market had become almost as large as that of the United States. In 2000, US GDP accounted for about 33 percent of the total GDP of all WTO members, and EU GDP accounted for about 31 percent. The EU share growth has increased in part as a result of enlargement. Japan accounted for about 10 percent of WTO GDP in 2000, but Japan has always been reluctant to assume a leadership role at the GATT/WTO.⁵ Thus, US power at the GATT/WTO has been on the decline, and cooperation with the EU has been increasingly necessary to governing the trading system.

Three Periods of Governance

1947–1972: US Hegemony. The United States, which produced about 45 to 65 percent of GATT GDP throughout this period, dominated the drafting of the original GATT rules and the organization's policies during its first two decades. While the EC was formed in 1958, it never accounted for more than 17 percent of GATT GDP in those early years. Moreover, as discussed below, in the 1960s (which marks the last decade of this broader period), the EC was still building institutional authority, capacity, and processes to speak with a single voice in global trade talks.

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Reflecting the size of its enormous market, the United States forged the GATT 1947 system, making some concessions to Britain (the GATT's second biggest market, with about 10 percent of GATT GDP). The GATT established a process for and rules about trade liberalization, but the rules allowed the United States (and all other contracting parties) to maintain specified roles for the state (described below), including those that permit states to engage in nonliberal patterns of behavior. Most of those characteristics mirrored US and British state economic institutions. If the other original contracting parties wanted access to the huge US and UK markets, they had no choice but to accept the rules of liberalization and vision of the state embodied in the agreement drafted by London and Washington. When the United States accepted the GATT 1947 rules, it had to legislate nothing and modify none of its state institutions. (Barton et al. 2006).

1973–1989: EC–US Duopoly Subject to a Cold War Constraint. By the 1970s, Europe was increasingly assertive in GATT negotiations. In 1973, the United Kingdom, Ireland, and Denmark joined the Community, raising the EC share of GATT GDP to about 25 percent. A Community that now included the big three European powers (England, France, and Germany) had to be reckoned with. Moreover, as explained below, the EC now had the institutional authority, capacity, and processes to participate effectively in GATT negotiations. By 1973, Gerard and Victoria Curzon could write that the EC had to be included in any successful initiatives at the GATT (Curzon and Curzon 1973). In the Tokyo Round (1972–1978), the most important multilateral trade roundup to that point, the EC and the United States worked together to set an agenda (i.e., the formation and drafting of texts that would be difficult to amend) that would define the final package of legal undertakings. The developing world obtained significant benefits in that trade round largely because the United States believed it was constrained by cold war competition with the Soviet Union from imposing harsher terms (Steinberg 2002).

1990–Present: Transatlantic Governance. With the collapse of the Soviet Union, cold war competition no longer constrained EC-US dominance of the global trading system. Moreover, the move of European political economies in a liberal direction in the 1980s and 1990s, and the Commission's embrace of a liberal agenda, helped the EC and

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United States overcome some of their traditional disagreements over trade policy. The World Trade Organization was established, and its rules were created, by agreements between the EC and the United States that were imposed on the rest of the world. Shortly after conclusion of the Uruguay Round in 1994, both the EC and the United States withdrew from the GATT 1947 system, disengaging from their most favored nation (MFN) commitment to developing countries. In the same period, the EC and United States entered into the Agreement Establishing the World Trade Organization, which included GATT 1994 (and its MFN guarantee) and required adherence to all the WTO multilateral agreements, many of which the developing countries had previously refused to sign—such as the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPs), the General Agreement on Trade in Services (GATS), and the Understanding on Balance of Payments. This legal-political maneuver—exercised as the “single undertaking” approach to closing the Uruguay Round—presented the developing countries with a *fait accompli*: either sign on to the entire WTO package or lose the legal basis for continued access to the enormous European and US markets.⁶

From the time the transatlantic powers agreed to that approach in 1990, they definitively dominated the agenda-setting process. Virtually all of the WTO agreements derived from proposals first formulated and texts first drafted through transatlantic consultations. Subsequent modifications to those texts took into account the preferences of other countries, but the fundamental substance and structure of those texts remained largely EC-US products (Steinberg 2002).

2. International Engagement and the Transformation of European Trading States

While Europe's market is one of the largest in the world, it would not have been able to effectively co-govern—or even participate effectively in—the GATT/WTO without a significant reorganization of the state at both the EC and member-state levels. That reorganization was favored not only by the exigencies of GATT/WTO co-governance but also by other demands of international engagement, such as the desirability of negotiating the terms of EC enlargement and the need to compete and cooperate with the United States, Japan, and other coun-

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tries on a bilateral basis. Much of the institutional development necessary for Europe's international engagement occurred in the 1960s and early 1970s.

Europe's increasingly unified role at the GATT/WTO, and its emergence as a leader there, parallels the emergence of its broader geostrategic role. The European Economic Community was established in 1958, most obviously to expand trade within Europe but also to help embrace and contain Germany within Europe. By the early 1960s, however, it was also clear that the EC was supported to create Western European unity in opposition to the Soviet Union; it was in that period that the EC was effectively seated at the GATT and began to intervene there on behalf of and usually instead of its member states (Jackson 1969). After the cold war, the challenge was to avoid a resurgence of German dominance by binding it to the rest of Western Europe, a goal that drove the establishment of the EU and monetary union; it was in this period that the EU acquired formal membership status (alongside the EU member states) in the newly created WTO and fully emerged as a coequal with the United States in governing the institution. This emergence of the EU as an active GATT/WTO member and partner with the United States in governing the GATT/WTO has been made possible by three important transformations of European state structure.

Shifts of Authority

The first change necessary for European co-governance of the GATT/WTO was a monumental shift of authority. If the EC were to bargain effectively at the GATT, it needed a single voice. This demanded a shift of authority upward, away from the member states to the Community decision-making level; laterally, from the member states acting through the Council to the Commission; and toward the Commission's trade group within the external affairs directorate from other groups and directorates. Similar authority shifts also took place within member states.

Article 113 of the Treaty of Rome gave the Commission exclusive authority to conduct negotiations with third countries "in consultation with a special committee appointed by the Council," and in this context, the Council was to act by qualified majority. When the Treaty

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of Rome entered into force, a special committee composed of the member states' most senior trade policy officials was established. In February 1959, this became the "113 Committee," but it remained undefined with no guidance as to its working practices, and the Commission did not then recognize the committee as an important institution of trade policy. Indeed, throughout the 1960s, the 113 Committee was reserved mainly for technical questions. Trade policy with third countries was instead coordinated by the Commercial Questions Group, a committee subordinate to the General Affairs Council, which subjected the Commission to precise speaking mandates from the member states and which jealously guarded member state control over Community trade policy. Consistent with this limit on Commission authority, some member states retained bilateral trade arrangements with non-Community countries well into the 1970s (M. Johnson 1998).

In the 1960s and 1970s, as the GATT trade agenda became more complex and as the EC negotiated its enlargement, the Commission developed its authority as the sole spokesperson for the EC. During the Kennedy Round (1964–1967), which was the first round to address trade topics that went beyond tariff reductions, the Commission began to articulate a need for the EC to speak with a single voice. That notion finally went unchallenged in the Tokyo Round (1973–1979), where the growing complexity of trade policy and broader range of topics made it increasingly difficult for Council ministers to understand detail and effectively broker deals with the rest of the world. By the early 1970s, the Commission ran EC trade policy, and the 113 Committee was consulted to help resolve competing member-state interests and priorities (M. Johnson 1998).

Within the Commission, authority over trade-related policy shifted toward the trade section of DG I (now called DG Trade). DG I/DG Trade coordinates European trade policy and takes the lead role in all EC negotiations with third countries. Moreover, the Commission's liaison with the 113/133 Committee⁷ has been coordinated since its inception through the international commercial questions directorate of DG I/DG Trade. In discussions with DG I/DG Trade over its central role, other Commission directorates have not always maintained a friendly or collegial stance. Until 1982, DG I acted as Commission spokesperson on all matters that came before the 113 Com-

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mittee; since then Commission officials with responsibility for policy that is of domestic and trade-related interest (e.g., agriculture, competition policy, and intellectual property protection) speak directly to the committee when those policies are raised, but DG I/DG Trade still coordinates the liaison (M. Johnson 1998; Nugent 2001).

These formal shifts of authority have had a big impact on who controls trade-related policy in Europe, for the effect has been to shift agenda-setting on trade-related issues from the member states toward the Commission, and toward DG I/DG Trade from other Commission directorates. As the scope of trade policy has expanded over the decades, from exclusively addressing tariff matters to now including such topics as agricultural subsidization, trade remedies laws, health and safety measures, environmental regulation, and services regulation, so has the scope of DG I/DG Trade's authority and influence over policy. Michael Bailey, Judith Goldstein, and Barry Weingast have shown how analogous shifts in the US trade policymaking process have shifted agenda-setting authority from Congress to the Office of the United States Trade Representative (Bailey, Goldstein, and Weingast 1997). Indeed, the establishment of congressional-executive trade agreements with ex post congressional approval is regarded by most legal scholars as a "silent" US constitutional amendment (Ackerman and Golove 1995; Tribe 1996).

A parallel upward shift has occurred within the member states. The member states retain influence over trade-related policy through their representatives on the 113/133 Committee. The 113/133 Committee now operates on three levels, that of the Principals, the Deputies, and the Titulaires. The member-state representatives at each committee level are from the central governments—not from member-state parliaments or subfederal levels of government—and usually from member-state trade or finance ministries (M. Johnson 1998; Murphy 2000). As the Commission often uses the 113/133 Committee to broker package deals on trade-related policy among the member states, the 113/133 Committee itself sometimes acts as an agenda-setter, which has the effect of shifting authority within member states toward the central government's trade or finance ministry and away from other ministries, parliament, and subnational levels of government.

For example, in Germany, there has not been a consistent trend in

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formal shifts of the balance of authority between the federal government and the *Länder*; but *informal* government practices have expanded the federal government's authority. Since enactment of the Basic Law of 1949, the federal government has been entrusted exclusively with the conduct of foreign relations, but treaties that regulate the overall political relations of the Federal Republic with other states or international organizations, or treaties that concern specified matters of legislation, require an Act of Consent by the two houses of the Parliament—including the Bundesrat, which represents the *Länder*. As a German constitutional matter, *Länder* governments have explicit authority over regional economic development (among other things), and most administrative matters (except defense, postal service, and foreign affairs), many of which have been delegated to local governments (e.g., economic public services, such as water and power supply).

The formal federal balance of authority in Germany has shifted back and forth over the last twenty-five years. The period of divided government that began in 1969 precipitated a 1974 decision by the Federal Constitutional Court. The ruling limited the Bundesrat's jurisdiction by denying its veto authority over bills that only revised existing programs. But in 1993, *Länder* politicians gamely managed to reverse their fortunes: in return for their support for two constitutional amendments needed to implement the Maastricht Treaty, they secured a veto over all future transfers of sovereignty that affected them and gained representation at the EU Council of Ministers meetings that addressed specified issues.

While these seesaw shifts in formal federal authority have been driven more by German and EC politics than by GATT/WTO pressures, the German state has taken action related to trade politics that has helped the federal government increase its authority over economic matters and the content of trade negotiations. Fears that the *Länder* were not able to respond to lost economic competitiveness, or to economic shocks associated with the free movement of goods, services, and labor, led to a substantial upward shift in governmental authority in the late 1960s and 1970s (Katzenstein 1987; Fukui et al. 1993). Moreover, as a practical matter, as the breadth of international trade topics has expanded to include such matters as subsidization, government procurement, and police affairs, the breadth of the federal government's authority has expanded as well. Perhaps most signifi-

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cantly, during the Uruguay Round, the federal government agreed with the European Commission to a “Code of Conduct,” which allowed the Commission to negotiate at the GATT in strict coordination with the Council and the member states via the 113 Committee. In this committee—as well as in the Council—Germany was represented exclusively by the Economics Department and the Foreign Office, without any direct participation by representatives of the *Länder* (Hilf 1997). Hence, the international negotiating process had included participation by the federal government to the exclusion of the *Länder*.

By retaining control over international negotiations and the package of outcomes contained in each international trade agreement, the German federal government has placed itself in the position of agenda-setter on substantive undertakings, able to logroll trade agreements that have a good chance of success in Parliament. The *Länder* are relegated to a position of after-the-fact veto players operating through the Bundesrat. As the topics of regulation considered at both the European and GATT/WTO levels have broadened, so has the effective authority of the federal government.

Development of New State Capacities

The second implication of the EC’s international engagement—including its emergence as an active participant in GATT/WTO trade negotiations—has been the development of new state capacities at both the European and member-state levels. Not only has the Commission developed great expertise on external trade relations in DG I/DG Trade; it has also built its capacity to use a host of policy levers to protect European industry.

The development of antidumping and countervailing duty law and associated Commission activity constitutes one such area of increased EC capacity. In 1968, based on the vague Article 113 mandate to establish a common commercial policy, the Community established through Regulation No. 459/68 that its institutions would have the exclusive capacity to erect “protection against dumping or the granting of bounties or subsidies by the countries which are not members of the European Economic Community.” Antidumping measures quickly became the most frequently adopted trade policy instrument after tariffs in the EC. The EC has targeted over forty-eight countries through

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over 1,000 proceedings since 1970 (Bael and Bellis 1990). In their regression analysis of commission antidumping and countervailing duty cases in the 1980–1987 period, P. K. M. Tharakan and J. Waelbroeck found that the larger the size and cohesion of the affected EC industry, the greater the chance that the Commission imposed an antidumping or countervailing duty, suggesting that these EC “trade remedy” policies serve to protect the strongest and most vocal EC economic interests. The same study also found that countries with which the EC had a short-term bilateral trade deficit were less likely than countries with which the EC had a short-term bilateral trade surplus to obtain a “softer” undertakings resolution of antidumping cases, suggesting that EC antidumping policy perhaps has been used partly for mercantilist purposes (Tharakan and Waelbroeck 1994).

EC competition law has also been implemented in a way that is intended to protect European industry or advance its competitiveness. Treaty of Rome Articles 85 through 90 (now Articles 81–89 in the EC Treaty, as amended) provide a basis for regulating activities that interfere with free market competition, a policy that could be consistent with the Treaty of Rome’s objective of ensuring the free movement of goods, persons, services, and capital throughout the Community. The operational basis for Commission regulation of alleged anticompetitive practices rests in Regulation 17, which was approved by the council in 1962. This gave DG Competition a firm procedural foundation to make inquiries and carry out investigations of alleged anticompetitive practices (Goyder 2003). In 1990, DG Competition’s competence was significantly enhanced by Council Regulation 4064/89, the Merger Regulation, which established clear guidelines for the regulation of firm mergers and acquisitions that might threaten to create excessive market concentration in Europe (Rivas 1999; Cook and Kerse 1991). However, unlike US antitrust law, which is now generally interpreted in line with the Chicago School’s objective of promoting free market efficiency, DG Competition implements its policy to advance both consumer welfare and “the competitiveness of European industry”⁸ (Wolff and Howell 1999). It may be difficult to show empirically how this latter policy objective affects Commission activity (Gerber 1998), but it suggests the possibility that the Commission may use its competition policy regulatory capacity for protectionist or mercantilist ends.

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The Commission has also developed a capacity to protect or grow particular sectors that might otherwise suffer from the Community's exercise in global trade liberalization through the GATT/WTO. The Common Agricultural Policy (CAP), which was inaugurated in 1962, has maintained farm income through price supports. While initially intended to appease French interests, the CAP has favored not only intra-EC agricultural trade but also expanded EC agricultural exports (Hurwitz 1987; Marsh and Swanney 1983; Steinberg and Josling 2003). Likewise, while the Airbus project was not launched under EC auspices, by the mid-1990s, it had become clear that the EU provided the only available political, legal, and financial framework in which all of the project's needs could be addressed. Consequently, the Commission created the Aeronautics Task Force, which coordinates the European aeronautics policy that supports Airbus (McGuire 1997; Hickie 1998).

State capacity at the European and member-state levels has also increased in ways intended to enhance the political palatability of European participation in the global trade liberalization exercise. Member states have long engaged in strategies of "domestic compensation," tendering generous early retirement benefits or retraining programs to workers displaced by international competition (Katzenstein 1985). Indeed, the expansion of Europe's massive welfare states has tended to go hand in glove with increased exposure to international trade (D. Cameron 1978; Rodrik 1997, 1998; Garrett 1998a).

An analogous development has been taking place at the European level. The EU deploys significant regional and structural funds to help alleviate the hardship of backward or struggling regions facing intensified competition. For example, European regional funds were doubled as part of the "1992" Single Market project. Today, they represent nearly 25 percent of the EU budget, the second biggest program after agriculture (which itself originated as a kind of compensation to France for accepting greater competition in industry). The capacity to offer such protection and side payments has helped make EU participation in GATT/WTO trade liberalization politically viable at home.

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Processes of Policymaking

A third implication of EU international engagement has been the development of new processes of policymaking within the EU and the member states. Some of these changes have been described above, but a few others deserve mentioning.

At the Commission level, global and bilateral trade bargaining have required increased consultation and coordination across directorates. Two reorganizations of intraCommission policy consultation are particularly notable, the first in 1993 and the second in 1999. In the Uruguay Round of trade negotiations (1986–1995), there was so much intraCommission conflict and difficulty in reconciling positions among the DGs (particularly DG I–External Affairs and DG XIII–Agriculture) that in 1993 the Commission adopted Rules of Procedure (hereafter the “1993 Rules”) to ensure cooperative efforts in policymaking. The Commission’s Manual of Operational procedures already specified that only one directorate should be the lead department on any proposal. The 1993 Rules noted that consulting directorates have no authority to insist that changes be made to a proposal prepared by the lead DG but established a formal mechanism for consultation among directorates over the formulation of trade policy and other policy. In 1999, Commission president Romano Prodi reorganized the constituent parts of DG I (the directorate responsible for external affairs) into four directorates (subsequently known collectively as RELEX), investing DG Trade with responsibility over trade policy, and provided for new mechanisms of coordination. These mechanisms included meetings of the four RELEX directors general (at least monthly); establishment of the Commissioners’ Standing Group on External Relations, which may be attended by non-RELEX commissioners when agenda items cover matters within their portfolios; and regular bilateral meetings between trade-relevant commissioners. While these procedural reforms have enhanced coordination, tensions still exist between DG Trade and other DGs, such as Agriculture (Bermann 1996; Nugent 2001; Pedler 2002).

Commission representation of Europe at the GATT/WTO and in bilateral negotiations has also necessitated the development of new nodes of direct interest articulation to the Commission. For example, the Trade Barriers Regulation, adopted in 1994, provides detailed

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rights and procedures by which industries and member states can require the Commission to investigate allegations of damaging barriers in third countries. This regulation is similar to the US Section 301 statute in that it formalizes the channels of complaint that are open to industry in the EU, empowers the Commission to decide whether there are grounds for the EU to take action (particularly legal action at the WTO), and requires the Commission to refer information about investigations to the 113/133 Committee, so that it can consider any wider implications for the common commercial policy (Murphy 2000; Shaffer 2003). Others have identified a myriad of means by which civil society may articulate its interests to the Commission in the process of developing Community trade policy (Moravcsik 1997).

EC international engagement has demanded clarification of the responsibilities of the Commission and the member states, respectively, in third-country trade talks. As explained above, in the EC's first decade, the political tension between commission and member-state control over such trade negotiations focused on which negotiating role would be performed by various EC institutions—the Commission, the Council, the Commercial Questions Group, or the 113 Committee. By the 1970s, it had become settled that the Commission would have the lead, but by that time, the breadth of “trade” negotiations began to expand, and the Commission–member-state tension began repeatedly reemerging and resolving through European Court of Justice (ECJ) decisions about the extent of the Commission's legal competence to act. In a string of decisions starting in 1971,⁹ the ECJ created and elaborated three categories of Commission competence to represent the EC area in trade talks. The Commission has *exclusive competence* to represent the EC area in negotiations over trade in goods, trade in services that are electronically transmitted, and trade rules that may affect an internal regime of the Community. The Commission has *no competence* to represent any of the member states on topics that are not within the competence of the Community to act, such as defense policy. And the Commission has *mixed competence* (and so must permit member-state diplomats to participate alongside it) on trade topics that raise issues both within and outside its exclusive competence, such as services trade (which raises, inter alia, extra-Community immigration issues) or member-state-financed commodity trading

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schemes (as direct member-state financing of such schemes is not within the Community's competence). In two of these decisions,¹⁰ the ECJ suggested a process for Commission–member-state coordination in mixed competence negotiations. Thus, not only has the process of EC–member-state coordination evolved in negotiations with third countries, but the ECJ has also offered a process for resolving questions about process.

Finally, EC participation in international trade negotiations has offered opportunities and incentives for change in the trade policy-making process within member states. For example, in France, as the scope of trade liberalization has expanded and its implications for the French economy have deepened, the trade policymaking process has changed. Since the 1970s, French trade policy was coordinated by an interministerial team created under the direction of the prime minister, led by the Ministry of Economics, Finance, and Industry (in which the Foreign Trade Ministry is housed), and including the Treasury and the Ministry of Foreign Affairs. In more recent years, as the impact of trade negotiations on the French economy has become obvious, the Direction des Relations Economiques Extérieures (DREE) was established within the Foreign Trade Ministry, and the head of the DREE has become the official French representative on the Article 113/133 Committee. In 2001, members of the National Assembly began demanding input into trade negotiations before they are concluded, and the National Assembly now maintains a committee that tries to watch over EC trade negotiations with third countries.

3. The Formation of Trading States on the Western, Industrialized Model

Once the EC had emerged as a substantial trading power, with the institutional capacity to wield that power, it was able to join the United States in co-governing the GATT/WTO system. The GATT/WTO rules promulgated by Europe and the United States may be seen as a cast of the Western, industrialized trading state (J. Ruggie 1983), which has molded the state in third countries in the image of that model.¹¹ Of course, the extent to which particular states have converged on the Western, industrialized model has varied.

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Casting the Western, Industrialized Trading State

What do GATT/WTO rules and principles, which were shaped by EC-US trade bargaining power, suggest about the state and the structure of the national political economy of each GATT/WTO member? Not surprisingly, they assume national political economies and state structures similar to those of the United States and Western Europe. GATT 1947 rules and principles presumed that the political economy of each contracting party would be fundamentally market oriented. The GATT was built on four cornerstones—MFN treatment,¹² national treatment,¹³ bound tariffs,¹⁴ and the elimination of quotas¹⁵—each of which could be undermined by the activities of state enterprises or state trading enterprises (Jackson 1989). For example, a state trading enterprise with a monopoly on all imports of a particular product could undermine the tariff binding on that product in the country where the enterprise operates: it could simply import the product, pay the tariff rate bound in that country's schedule of concessions, then internally resell all units of the product at a markup that exceeded the tariff paid for each unit. Hence, while GATT 1947 negotiators expected that some contracting parties might maintain state enterprises, Article XVII was written to severely constrain their activities, so that decisions would be taken according to purely commercial considerations (Wilcox 1972). Yet that solution has not always been considered sufficient, and the accession of some countries has been delayed or denied until there was convincing evidence of a trend and commitment toward drastic reduction in the role of the state in the economy (Steinberg 1998; Clarke 1993).

GATT contracting parties were also expected to have relatively few monopolies or oligopolies engaging in anticompetitive practices. Just as large monopoly state enterprises could undermine the four cornerstones, so could sizable private monopolies. For example, anticompetitive distribution networks could behave in ways that created a barrier to trade, with effects similar to tariffs, quotas, or denial of national treatment. Such arguments have frequently been leveled at the Japanese *keiretsu* and the Korean *chaebol* systems (Tyson 1992). The Havana Charter, an expanded form of what became the GATT, included express provisions against "restrictive business practices," and while the Havana Charter never came into being, a shared European-US

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norm against anticompetitive practices sufficed to limit political friction over the issue until Japan emerged as a significant economic power in the 1980s. Since then, the United States, the EC, and other GATT/WTO members have used GATT-legal national laws and agencies aimed at “unfair trade practices”—such as antidumping law—to offset and pressure countries that tolerate anticompetitive business practices.

In addition to capacity to act against anticompetitive practices, constituent states have been permitted by the GATT 1947 to maintain other capacities—regardless of their trade-limiting effects. GATT Article XXI permits the state to perform military security functions without constraint. Article VI, Article XVI, and related rules contemplate that the state may maintain simultaneously agencies that actively subsidize certain sectors (e.g., agriculture and commercial aircraft)—and agencies that monitor and act against other excessive subsidies by foreign governments. Moreover, in requiring “specificity” in order to challenge foreign subsidies, GATT negotiators have carefully permitted states to pursue broad social welfare and social safety net programs, which are presumed to be common to GATT/WTO members and crucial to their domestic politics. Article X, requiring transparent publication and adjudication of disputes over trade regulations within each contracting party, demands in effect that constituent states maintain an operational judicial system. And the Article XX exceptions show that constituent states are expected and permitted to maintain agencies to protect consumers, the domestic environment, public morality, and intellectual property. The Tokyo and Uruguay Rounds further defined GATT/WTO rules and principles and expressly acknowledge the role of constituent states in regulating various service sectors, including telecommunications and financial services.

Not every GATT/WTO member state was expected to be structured precisely along the lines suggested by the regime’s rules and principles. For example, derogations have applied to the least developed countries. And some countries, such as France and Japan, were able to conduct significant state economic intervention without substantial foreign complaint until their economies became large enough to threaten the interests of other powerful contracting parties (S. Cohen 1998). These exceptions aside, GATT/WTO rules and procedures have been drafted with a particular range of permissible state

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structures in mind, structures that reflect those of the United States and Western Europe.

Molding the State in Third Countries: State Change Favored by GATT/WTO Rules

GATT/WTO rules and principles have provided opportunities and incentives for the transformation of the state, particularly in newly industrializing countries. As suggested above, the agenda-setting that led to the GATT 1947 and the 1995 WTO agreements was dominated by the United States and Europe, establishing agreements that demanded relatively little immediate legal or institutional change in either territory. Yet for most other countries, particularly midlevel developing countries, the procedural and substantive requirements of joining and participating in the GATT/WTO, and the incentives and opportunities created by the regime, have required or favored substantial change in state institutions.

There have been powerful economic incentives to accede to the GATT/WTO system. Nonmembers suffer trade and investment diversion (Viner 1950) and risk losing access to the world's largest markets (Steinberg 2002). As the GATT/WTO started to grow and integration among its members deepened, so did these costs of nonmembership, creating a bandwagon effect (Barton et al. 2006). Accession also promised to buttress the domestic political position of liberal-minded reformers in developing countries that had embraced import-substitution-industrialization policies and transitional economies that had pursued central planning (Goldstein 1996). Hence, the regime grew from 22 members in 1948 to nearly 150 members by 2005.

For most states with significant internal markets, GATT/WTO accession necessitates not only policy changes, sometimes referred to as "paying the price of admission" (Jackson 1969), but also institutional changes in the acceding state. For example, consider the substantive and institutional demands of implementing just one of the GATT/WTO agreements—the TRIPs. TRIPs requires each WTO member to enact substantive laws guaranteeing protection for patents, copyrights, trademarks, and know-how. It also mandates the establishment or maintenance of various state institutions, such as a patent office.

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Moreover, by requiring that each WTO member offer “effective means” of enforcing intellectual property protection through injunctive relief, civil actions, and other enforcement mechanisms, the agreement demands that states maintain court systems that operate according to the rule of law. Institutional form follows function. Failure to adhere to TRIPs on substance or form makes nonadherent members susceptible to the WTO dispute settlement system, which can ultimately subject such states to trade sanctions for noncompliance.

As GATT/WTO liberalization has deepened, so has the scope of the demand for state institutional change among members. Over time, the scope and scale of GATT/WTO obligations have increased. This increase is reflected in the size of GATT/WTO accession protocols: in 1951, the Model Protocol of Accession to the GATT was 4 pages and required adherence to the GATT and the acceding country’s schedule of tariff concessions; in 2001, China’s Protocol of Accession was over 50 pages and required adherence to the GATT, China’s schedule of tariff concessions, its schedule for services liberalization, approximately 300 pages of additional WTO agreements, and the rules and principles established in GATT/WTO dispute settlement decisions. The GATT 1947 and subsequent multilateral trade negotiations prior to the Tokyo Round addressed largely border measures, such as tariffs and quotas. Since the 1970s, however, GATT/WTO agreements have concentrated increasingly on behind-the-border issues, such as services regulation, health regulations and industrial standards, and intellectual property rights. The Doha Round of negotiations initially added investment regulations, competition policy, and environmental regulation to the agenda, suggesting a host of new issues for the future trade agenda. As multilateral integration has deepened, the demands on GATT/WTO member states have increased.

In third countries, the extent of state change to comply with the GATT/WTO terms of integration depends on the starting point. The trade regime’s pressure on states to adapt in a functional manner is mediated by particular national histories and strategic choices. However, empirically, in third countries, a country’s level of economic development is the most important determinant of the extent of state institutional change associated with GATT/WTO membership. Such change has been least extensive in the least-developed countries (LDCs), such as the Democratic Republic of Congo and Lesotho; in

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these countries, most of the demands of the GATT/WTO system have been formally suspended or simply not enforced, largely because their markets are too small to matter to US and European business interests. Moreover, in most LDCs, state institutional capacity and political authority structures have not reached a threshold at which trade regime demands would have any meaning. In some of the poorer developing countries, such as Ghana, there has been significant change in the form of the state, but it is not clear to what extent such change may be hollow in the sense that many state institutions may be unable to perform the functions for which they were organized (Meyer et al. 1997).

The opportunities and incentives embodied in the GATT/WTO agreements have precipitated the most state change in developing countries. In these countries, GATT/WTO rules have favored a bounded convergence toward some aspects of the US/Western European and GATT/WTO model of the state along five dimensions:

1. *Reduced role for state-led and central planning institutions.* GATT/WTO trade liberalization and the trade and investment diversion suffered or feared by those countries outside the GATT/WTO system have favored reducing the state's direct role in domestic economic planning—central planning, state trading enterprise systems, state-owned enterprises, and state-led capitalism.

2. *Elements of new state capacity.* At the same time, the GATT/WTO (a) expressly permits, employs, and disciplines increased regulatory capacity over sectors once controlled by—and fallout from—dismantled state trading and state-owned enterprises (especially over competition, financial services, telecoms, labor policies, etc.) (S. Vogel 1996); (b) provides opportunities (that combine with strategic trade goals to become incentives) for strategic trade institutions that can administer antidumping, countervailing duty, and safeguards laws, technology policy (but not industrial policy), export promotion capacity, and technical standards and testing; (c) requires (or is moving toward requiring) the establishment and maintenance of state institutions supporting intellectual property rights, environmental protection, and labor rights; and (d) favors the establishment of capacity for addressing internal spillovers from liberalization—internal revenue generation (to replace revenue previously generated from duties), a social safety net that can address dislocations associated with liberali-

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zation, and more technical standards and testing (to protect consumers, workers, and the internal environment from damage from imported goods).

3. *Shifts of authority.* The GATT/WTO has required or created incentives for shifts of authority within the state. While formerly state-led and central planning systems have experienced diminished state authority over the economy, in other countries, authority over the economy has in some ways become more concentrated in the state: (a) in federal systems, from subfederal levels to the central government (so that the state can negotiate with a single voice and comply with international obligations); (b) in presidential systems, from the legislative to the executive branch (so that the executive can bargain credibly and secretly); and (c) to trade ministries from other ministries—or to the external affairs division of trade and industry ministries—as previous domestic topics, such as intellectual property, environment, and labor, have become objects of trade negotiations.

4. *Changes in national policymaking processes.* Shifts in state capacity and the concentration of authority demand new processes of policymaking. For example, if authority over a particular policy shifts from one agency to another, then the processes of policymaking must also shift, so that nonstate actors can articulate their interests to the new authoritative policymakers. Similarly, if authority over a particular policy becomes shared by two domestic institutions when it was previously controlled by one, policymaking processes must shift, so that the institution previously at the center of a policymaking processes can participate in the new and expanded process. As the range of issues that are the subject of GATT/WTO negotiations has expanded, the domestic institutions of trade policymaking have adapted, so that broader sets of interests can feed into the trade policymaking process.

5. *National legal system changes.* The process and outcomes of GATT/WTO trade liberalization have favored and been accompanied by (a) an expansion in constitutionally acceptable forms of international agreements (e.g., in the United States, from treaties and executive agreements to congressional-executive agreements); and (b) marginal increased rule of law along some dimensions—formalization, transparency, and independent judicial review (e.g., all are required by GATT articles, TRIPs, and accession agreements).

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4. Conclusion: The Prospects for Continued Transatlantic Duopoly and the Future of European State Structure

The international system has shaped national political economic structures in ways that are historically contextual (Gourevitch 1978; Tilly 1975; Gerschenkron 1962). Global trade liberalization in the postwar period has assumed a distinct institutional form embodied in GATT/WTO law and characterized by a process of lawmaking that has depended crucially on EC-US cooperation and power (Steinberg 2002, 2004).

For the last thirty years, no single GATT/WTO member has had the power to unilaterally dictate outcomes. Without EC-US cooperation and power, change in GATT/WTO law would have required cooperation and a convergence of interests among dozens of countries with highly varied demographics, histories, and levels of economic development. Even if such cooperation could have taken place, the resulting growth of global trade would likely have been far more modest than we have seen. A successful conclusion of the Uruguay Round, the establishment of the WTO, and the launching of the Doha Round would have been hard to imagine. Development of the GATT/WTO multilateral system would have been stunted.

The transformation of European state institutional authority, capacity, and processes has been necessary for the EC to cooperate effectively with the United States in GATT/WTO negotiations. This chapter has identified the main elements of that state transformation in Europe. Monumental shifts of authority were necessary before the EC could speak with a single voice at the GATT. New EC and member-state capacities were developed to provide policy tools that could make regional and global liberalization more politically palatable at home. And those shifts in authority and capacity required changes in policymaking processes. As suggested by the battle in the 1960s and 1970s over EC authority for negotiating third-country trade agreements, many alternative institutional arrangements were imaginable. The outcome we have witnessed was not foreordained. The commission and the member states have made, and continued to make, choices to transform the organization of the trading state in Europe.

Will the EU and United States continue to dominate bargaining and outcomes at the GATT/WTO? The EU and US markets are the

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source of their dominant power at the WTO. Chinese and Indian economic growth, along with expansion of WTO membership, will likely erode that dominance. But the historically slow pace of change in the relative size of EU and US markets, indicated in Figure 9.1, suggests that power will shift slowly at the WTO—barring an unforeseeable catastrophic shock. In the short term, the bigger challenges to EU-US dominance at the WTO would seem to be from a potential divergence of EU and US interests, which Sylvia Ostry has identified as a basis for a possible “New Geography” at the WTO (Ostry 2004). Another risk is that the EU fails to continue transforming itself in ways that make its central governmental institutions effective (Tsebelis and Yatağan 2002), thereby reducing Europe’s ability to contract credibly at the global level.

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9. The Transformation of European Trading States

Parts of this chapter are excerpted from Barton et al. 2006 and Steinberg, 2007.

1. "EC" is used herein to refer to the European Community, the European Communities, and the European Economic Community. "EU" is used here in all contexts where reference is made to either the EU exclusively or the EC and the

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EU, over the course of their respective histories. These acronyms are used for purposes of simplicity and in accordance with convention in this book, despite the fact that the European Union did not exist before 1992 and the EU is not a member of the WTO. The European Economic Community was seated at GATT meetings from about 1960 (Jackson 1969). The European Communities became a member of the WTO at its inception.

2. For a more detailed account of these arguments, see Barton et al. 2006.

3. Calculated from International Monetary Fund 1977.

4. Calculated from World Bank 1972.

5. Many have speculated why Japan has not assumed a leadership role at the GATT/WTO. Perhaps the Japanese government is reluctant to lead global market liberalization efforts because Japan's own market has been relatively closed. It is also possible that Japan's ultimately unsuccessful effort at exercising global power in the first half of the twentieth century has left it with a cultural legacy biased against reassertion of leadership.

6. At that time, the combined EU and US markets accounted for approximately two-thirds of GATT/WTO GDP (World Bank 2001).

7. The articles of the EC Treaty have been renumbered so that Article 113 of the Treaty of Rome is now Article 133 of the EC Treaty, as amended. Accordingly, the relevant committee has been renamed the 133 Committee. References to the "113/133 Committee" refer to either the 113 Committee or its successor.

8. This statement appears on the EU's official Web site, in "Citizen's Guide to Competition Policy": <http://europa.eu.int/comm/competition/index-en.html#5>.

9. *Commission of the European Communities v. Council of the European Communities*, Case No. 22/70 (decided March 31, 1971) (where the Community has adopted internal rules in a given field of activity, external negotiations that may affect that internal regime are within the exclusive competence of the Commission); Case No. 1/76 (decided April 26, 1977) (where a power exists for the Community to adopt internal rules, relevant external negotiations are within the exclusive competence of the Commission, even though the Council may not have yet exercised the initial internal rule-making); *International Rubber Case*, Case No. 1/78 (decided October 4, 1979) (the Commission has exclusive competence to negotiate agreements that are essentially commercial in nature but only "mixed competence" to negotiate agreements that commit member states to directly finance it); and Case No. 1/94 (decided November 15, 1994) (placing each of several trade negotiating topics into one of three categories, Commission exclusive competence, mixed competence, and no competence).

10. *International Rubber Case*, Case No. 1/78; Case No. 1/94.

11. The "cast" and "mold" terms are used here as metaphors. Neither the cast nor the mold is perfect. As stated elsewhere herein, there is merely bounded convergence in the form of the state, suggesting that there is variance in the extent to which the trading state is converging on the Western model.

12. The MFN principle generally prohibits measures that discriminate against imports from one GATT/WTO member in favor of like products imported from another member.

13. The national treatment principle generally prohibits measures that discriminate against imports in favor of domestically produced like products.

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14. The GATT generally limits the tariffs that may be charged on a product to the level established for that product in each country's schedule of concessions. Tariffs so limited are said to be "bound tariffs."

15. GATT Article XI generally prohibits GATT/WTO members from maintaining quantitative restrictions on the importation of any good.

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