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REGULATORY SHIFT: THE RISE OF JUDICIAL LIBERALIZATION AT THE WTO

by

JUDITH L. GOLDSTEIN
STANFORD UNIVERSITY

and

RICHARD H. STEINBERG
UCLA SCHOOL OF LAW

Regulatory Shift:
The Rise of Judicial Liberalization at the WTO[*]

Judith L. Goldstein
Stanford Department of Political Science
and
Richard H. Steinberg
UCLA School of Law

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Introduction

International trade transactions are among the most regulated activities in the world. Indeed, the history of international trade since the 17th century cannot be understood without accounting for the changing ways by which public authority has interacted with, and influenced, private transactions (Heckscher 1922; Pahre 2007). In the contemporary era, we have witnessed a significant change in the locus of that regulation, from country specific policies to rule setting on the global, multilateral level, primarily through the emergence and evolution of the GATT and the WTO (Barton et al. 2006).

A specific change in global regulation has taken place in recent years. We argue below that the form of global rule setting has shifted, even as it has remained within the GATT/WTO. In the early years of the institution, trade regulation occurred through a negotiated legislative process associated with trade rounds. Over the last fifteen years, however, the focus of GATT/WTO trade regulation has moved from trade rounds to a judicial process. This shift is attributable largely to the increasing participation of developing nations in WTO negotiations, which has not only deadlocked the legislative process that for half a century liberalized global trade, but has also dampened the legislative check on judicial lawmaking. It is a shift that is consequential and not likely to be reversed anytime soon.

The differing effects of regulation by different branches of government is a well-mined topic in both political science and law. One line of scholarship has contrasted regulation by courts with regulation by administration or legislative bodies, evaluating their relative affects according to metrics like economic efficiency, optimal deterrence, and justice (Vogel 1986; Kagan 2001; Rose-Ackerman 1991). Others have explored conditions for regulatory capture at the national level by particularistic interests, an idea taken to the international level in this volume (Mattli and Woods 2007). We argue here a middle ground: the regulatory shift taking place at the WTO, from the legislative to the judicial, has increased the efficiency of the organization and enhanced open trade by freeing member states from capture by entrenched domestic interests.[1]

What explains this regulatory shift at the WTO? Although created with great hope and fanfare in 1995, the WTO has been unsuccessful at advancing a broad legislated trade deal among members. In the last decade, creating a consensus among WTO members has become increasingly difficult. Developing nations, often speaking as a bloc, have exacerbated disjuncture in U.S. and EC preferences on trade policy. The result has been an impasse at the negotiating table and little progress in the current Doha Round. These same divisions, however, help explain the increasingly active role being played by the Appellate Body. Legislative gridlock and judicial lawmaking may be related phenomena in the domestic or international context (Tsebelis 2002; Garrett and Tsebelis 2001; Burley and Mattli 1993).

The failure of multilateral negotiations has quietly ceded authority to an alternative institution for regulation. We argue that in the wake of failed trade negotiations, WTO lawmaking has moved out of the legislative venue of member states and into the courtroom. Delegation to the judiciary, established with the creation of the WTO, has been unexpectedly accompanied by considerable agent slack.[2] The same divisions that have undermined trade talks have made it increasingly difficult for the membership to provide a check on judicial lawmaking. As the prospects for legislative lawmaking have declined, judicial lawmaking has become more common, especially through interpretation of unclear rules and the filling of gaps within WTO agreements. Judicial lawmaking has been particularly evident in cases challenging subsidies or countervailing measures, antidumping duties, and safeguards measures, with considerable effect on the steel and agriculture sectors.

[1] We do not argue that market-opening will always move states away from capture. For example, in sectors characterized by high barriers to entry and declining marginal costs, market opening could favor cartelization.

[2] Our basic delegation model is drawn from Moe (1984), who argues that "the principal-agent model is an analytic expression of the agency relationship, in which one party, the principal, considers entering into a contractual relationship with another, the agent, in the expectation that the agent will subsequently choose actions that produce the outcomes desired by the principal." (756). We assume that the relationship between the GATT/WTO and its principals, nations or customs territories, always held some degree of a principal-agent relationship, although the membership exerted far more oversight over the agents (the secretariat or the dispute settlement panels) than is common with other international agencies.

Taken together, these developments suggest that we are entering a period of "judicial liberalization" at the WTO, led by the Appellate Body. As discussed in the conclusion, this development may have some parallels to the period of "negative harmonization" in the EC, led by the European Court of Justice (ECJ) from the mid-1960s through the mid-1980s, when the Luxembourg Compromise and more limited availability of qualified majority voting constrained harmonization through Council directives.

To examine the relationship between judicial lawmaking and legislative paralysis, we proceed in four steps. Our first section examines the collapse of the legislative process: the origins of and explanation for the contemporary legislative stalemate in the WTO. Our second section examines the dispute settlement system and argues that is has become an increasingly and unexpectedly important venue for lawmaking with a liberalizing bias. Our third section argues that this lawmaking has operated to free WTO members from capture by entrenched domestic protectionist interests in a way that negotiated liberalization efforts may not be able to do. Fourth, we explain why WTO judicial liberalization persists, suggesting that it may be favored by developing countries that now join together to block WTO legislative proposals that would diminish the Appellate Body's agent slack. Hence, we suggest that the decline in consensus at the ministerial level and the rise of judicial lawmaking are related and have made trade policy less prone to capture by protectionist interests.

(I) Liberalization Through Negotiation (1947-95) and the Emergence of Legislative Deadlock

The GATT/WTO created a rule-based system, which facilitated the worldwide lowering of trade barriers and the growth of world commerce (Goldstein et al 2007). The efficacy of the regime, however, rested on a consensus among its largest members. In its earliest years, the GATT/WTO reflected U.S. power; as U.S. market share receded, the organization continued to prosper because of a trans-Atlantic bargain between Europe and the United States. However, after 1995, as the transatlantic powers began demanding reciprocity from the South and accelerated their conclusion of preferential trade agreements (PTAs), consensus building became increasing difficult.

The basic design:

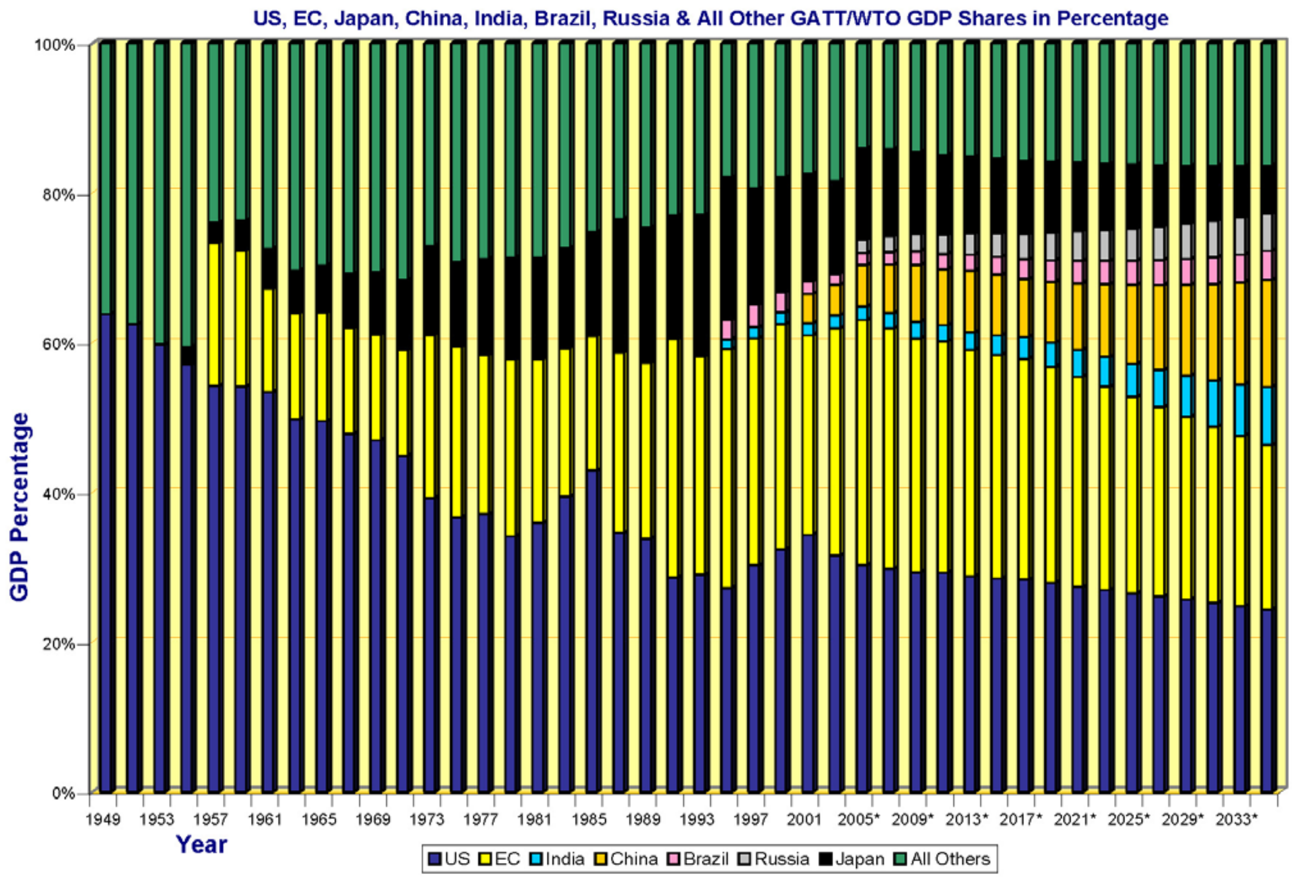
The GATT/WTO was created to solve what Bagwell and Staiger (1999, 2002) identify as a terms-of-trade driven Prisoners' Dilemma. According to this logic, large nations have an interest in shifting the cost of their trade protection on to their trade partners, therefore depressing foreign export prices and improving their own terms of trade. The problem, however, is that when all nations pursue this strategy, it gives rise to great inefficiencies: too much trade protection is produced and too little market access is available for growth. The literature on regimes points to a variety of ways in which international cooperation can change this individual calculation of interest. (See, e.g. Keohane, 1982). In the case of trade regimes, the problem was ameliorated through the adoption of two fundamental principles: most-favored-nation (MFN) and reciprocity. These principles, however, did not equally affect the behavior of all members. Only those nations with large markets participated in the reciprocal lowering of tariffs, initially through the mutual exchange of benefits between principal suppliers of goods. Through a process of horse-trading market access in one set of goods for another, the large nations ratcheted down their tariff levels. This focus on the large markets is consistent with the explanation for the origins of the regime given by Bagwell and Staiger, since the terms of trade dilemma exists for a country with a market that is large enough to set the world price in a product.

Of course, the regime was created to include both big small nations. At its inception in 1947, half of the nations at the Round were developing and not developed countries. These nations also benefited from regime participation but via the MFN provision in the GATT/WTO. Even in the absence of a commitment by the developing world to increase access to their own market, the MFN provision assured them of new export markets. Some Southern countries did liberalize their markets in the pre-WTO period, either in a Round or in the process of accession, but the majority of these GATT members eschewed liberalization at home and grew their foreign trade through MFN-garnered export access.

Reliance on a norm, reciprocity (at least among big countries), and a rule, MFN, to fuel trade liberalization had long-term implications. The reciprocity norm made bargaining power in the GATT/WTO a function of market size and a nation's willingness to use the threat of market closure as a means to influence others. Figure 1 shows actual market size (measured in GDP) of the biggest GATT/WTO members from 1949 through 2004, and projected market size from 2005 through 2034, as a percentage of GATT/WTO market size.[3] In the GATT's early years, U.S. GDP accounted for about 65% of GATT

[3] National GDP figures for 1949-2004 are from the World Bank; they were converted into U.S. dollars at the annual average prevailing exchange rate, using IMF data. World Bank 2005; International Monetary Fund 2005. Projected figures for 2005-2035 assume rates of national GDP growth for the largest WTO members that similar to those used by the Global Economics group at Goldman Sachs (Wilson and Purushothaman 2003). The Goldman Sachs model predicts growth as a function of growth in employment, growth in the capital stock, and total factor productivity (TFP) growth. The latter is modeled as a process of catch-up on the developed economies. The Goldman Sachs model forecasts for GDP growth in the next ten years are similar to IMF estimates of potential growth in the economies evaluated here (IMF 2005). Its projections are also close to those using the Levine and Renelt econometric model that explains average 30-year GDP growth as a function of initial per capita income, investment rates, population growth, and secondary school enrollments (Levine and Renelt 1992). We adjusted the Goldman Sachs growth rate projections downward for China and Russia in order to be conservative and to countervail implicit assumptions in the model about stable domestic political institutions and sound macroeconomic policies in those countries. Specifically, for China we assumed two shocks, one in 2010 (that would reduce growth from around 8% to 0% for that year, 3% in 2011, and 7% in 2012) and a large political shock in 2015 (resulting in -5% growth that year, returning to projected levels by 2019). For Russia, we assumed only the former shock.

Figure One:



GDP; the United Kingdom accounted for another 10%. Since then, the relative size of the U.S. market has consistently declined; starting in 1957, that of the EC has grown.

Shifting market share parallels coalition behavior in the GATT. The early years, 1947 to 1973, were a time of almost complete economic dominance by the United States. While the EC's market share was growing, it only accounted for an average of 15% of GATT GDP during the period. The establishment of the GATT itself best exemplifies

U.S .dominance of the GATT negotiating process in these early years. The United States drafted the instrument that became the GATT 1947. It made accommodations to the United Kingdom, enabling the maintenance of colonial preferences, but the General Agreement was fundamentally U.S. designed (Barton, et al. 2006).

By 1973, the U.S. share of GATT GDP had fallen below 40% and the EC share had grown to more than 20%. Other changes had occurred in the interim. Before 1973, EC institutions were insufficiently developed to enable Brussels to partner with Washington to govern the GATT system. By the mid-1970s, however, the role of the commission in coordinating Europe's external commercial negotiations, and that of the 113 Committee in overseeing the Commission, were clearly established, enabling the EC to speak with a single voice. (Steinberg 2006). As a result of both shifting market shares and better coordination among EC members, Brussels and Washington began regular bilateral consultations, often followed by an expanded conversation among the "Quad Group," which also included Canada and Japan. Decisions of the "Quad Group" were then often presented as a *fait accompli* to the other GATT contracting parties. By the early 1970s, commentators had begun to suggest that US-EC cooperation was necessary for successful negotiations at the GATT (Curzon & Curzon 1973.)

The power of this coalition is exemplified by the events surrounding the establishment of the WTO. In 1991, the EC and United States decided to impose the results of the Uruguay Round negotiations on the rest of the world through what they initially referred to as "the power play." Specifically, they agreed that they would withdraw from the GATT 1947 and sign a substantively identical but legally distinct instrument, the GATT 1994. This would disengage Europe and the United States from their GATT 1947 MFN commitments to the rest of the world, and would replace them with new MFN commitments in the GATT 1994. The EC and U.S. negotiators agreed that these new commitments would be conditioned on third countries' acceptance of all the WTO multilateral agreements. The effect of this maneuver was to threaten closure of the world's two largest markets (those of the EC and the United States) to any country that did not accept *all* of the WTO multilateral agreements-- including the Agreement on Trade-Related Intellectual Property Rights (TRIPs), the General Agreement on Trade in Services (GATS), the Understanding on Balance-of-Payments Provisions of the GATT 1994, and other agreements, which most developing countries had previously refused to accept (Steinberg 2002). This transatlantic maneuver, which became known diplomatically as the "Single Undertaking" approach to closing the Uruguay Round, allowed the EC and United States to set the terms of the new organization. Now, all the regime's principles, through a more general interpretation of MFN, would be applicable to the developing world.

The creation of stalemate:

For those favoring rapid and deeper liberalization, the WTO's biggest contemporary problem is an inability to gain consensus on a negotiated outcome. Stalemate in multilateral trade negotiations is the order of the day. Three developments explain the creation of stalemate.

First, in recent years the norm of reciprocity has become generalized across all countries. Robert Hudec showed that throughout most of GATT history, North-South negotiations were characterized by non-reciprocity-- an absence of expected reciprocity from poorer countries-- a norm that he speculated might have started breaking down in the mid-1980s (Hudec 1987). As of 1994 the norm of non-reciprocity became the exception, not the rule. Before then, the GATT made policy through an implicit bargain between the developed and the developing world. The Northern countries opened up their markets but only in the range of products of their choosing; the South gained access to Northern markets without having to give reciprocal access. The cost of this deal was that the South could not choose what products gained access. In the 1970s, the GATT responded to the growing economic gap between the groups by expanding the number of preferences granted to developing nations, allowing access over and above that offered by MFN.

At the same time, starting in the 1970s, and increasingly by the mid-1980s, powerful constituencies in the North were demanding deeper liberalization that would discipline behind-the-border measures in such areas as technical barriers to trade, services regulations, and intellectual property protection. Moreover, as the U.S. trade balance deteriorated and the Asian Tigers emerged, various groups in the United States began demanding reciprocity from all countries. With this change in the focus of the trade regime and U.S. demands for a "level playing field," the North-South bargain became unstable. In return for agreement on a set of new rules, a developing world bloc began asking for changes in the negotiating agenda, especially for negotiations on a range of goods of their choosing. Unable or unwilling to offer much in return, negotiations have become attenuated and increasingly difficult.

Second, developing countries have adopted institutional strategies to sustain their coalitional behavior. Trade negotiations have always been difficult, and developing countries have in the past episodically joined together to influence negotiations. But the sustenance of contemporary developing country coalitions is unprecedented. Developing countries are continuously acting in concert with each other, sustaining blocs that have successfully vetoed a range of various proposals favored by the EC and United States.

The developing countries are not a unified bloc with identical interests, but they have figured out an institutional solution to remaining more unified and cohesive than ever before. Specifically, they are agreeing to bundle issues together, creating linkages across the interests of varying types of developing countries. In trade negotiations, efforts by countries to sustain a common and unified position on a single issue are unstable, susceptible to the “divide the dollar” problem. When a position is taken on a single issue by two or more countries, a third country may offer a coalition member a more attractive commercial concession to catalyze withdrawal from the common position. This was a common problem for the EC and United States in the early years of the Uruguay Round. For example, the EC and the United States had taken a common position in the TRIPs negotiations on the single issue of protecting pharmaceuticals in the regulatory pipeline; India was able to pry apart that coalition by offering the EC a politically valuable tariff concession in exchange for its shift of position on the pipeline issue. Europe and the United States solved the problem of being split asunder by agreeing to bundle issues, taking a common position on a host of issues of interest to each of them. In the Uruguay Round, the developing countries did not bundle and they were frequently frustrated in efforts to take a common position on individual issues.

In the Doha Round, the South seems to have learned this lesson. For example, the G-77 plus China took a common position opposing negotiation on issues such as competition policy, the environment, labor, and investment, and agreeing to support Northern country industrial tariff and agricultural subsidy cuts, aid for trade, and access to medicines. The Africa Group meets annually to determine the set of issues that it will bundle together; Dr. Supachai has said that he is using his leadership of UNCTAD to help coordinate this bundling, with the knowledge that it is crucial for the cohesiveness of the Africa Group in the Doha Round. Similarly, the Newly Acceding Group of Countries in the G-20 has also done some bundling.

Since 1995, the developing world has been more successful than ever before at ending Northern hegemony of the GATT/WTO system. Although not able to force the developed world into compliance to their wishes, they have become effective veto-players, a role they have repeatedly played with success in the Doha Round. In other episodes of GATT/WTO history, developing countries have also displayed unity, particularly when they successfully blocked conclusion of the Tokyo Round negotiations unless they were given a free ride on the MTN agreements (which were concluded as codes and accorded MFN treatment). But until the Doha Round, the developing world never sustained cooperation in both the early and middle stages of a Round, when the agenda is typically set and the texts of the agreements themselves are being negotiated.

Third, beginning in the 1990s, the EC and then the United States began accelerating their conclusion of PTAs, which has had the apparently unintended and unanticipated consequence of diminishing their bargaining power at the WTO. Largely in pursuit of a strategy of "competitive liberalization," the conclusion of PTAs became a cornerstone of EC and U.S. trade policy in the 1990s. In one version, "competitive liberalization" resulted from a belief that trade liberalization at three levels-- multilateral, regional, and bilateral-- would be necessary for developing countries to implement economic reforms. In another version, "competitive liberalization" meant that bilateral PTAs with a hub-and-spoke architecture concluded by the EC, on one hand, and United States, on the other, would pressure excluded third countries (by operation of trade and investment diversion) to also demand PTAs with Washington and Brussels; eventually, the idea was that eventually the terms of these PTAs could be multilateralized at the WTO. (Bergsten 1996; Zoellick 2000; Bhala 2007). By mid-2006, the EC had concluded nearly 40 PTAs, with additional negotiations underway to convert the Lome Agreement into a set of reciprocal free trade agreements covering an additional 73 African, Caribbean, and Pacific countries. By the same time, the United States had concluded PTAs covering trade with fifteen countries, covering nearly one-third of total American trade, and was negotiating to conclude more.

As far as we can tell, neither Washington nor Brussels fully appreciated ways in which the strategy of competitive liberalization could backfire on multilateralism and make progress at the WTO more difficult. It is one thing to conclude a bilateral deal between Washington (or Brussels) and a smaller country; it is quite another to multilateralize its terms with a third country like China. Moreover, the PTA strategy accompanied a new intransigence on the part of the EC and United States in the Doha Round, in part a function of the availability of an alternative to WTO liberalization. Most importantly, however, the conclusion of these PTAs has diminished EC and U.S. bargaining power at the WTO by providing bilateral MFN guarantees to PTA partners. Legally, the proliferation of EC- and US-centered PTAs has fatally constrained the ability of Europe and the United States to behave as hegemonic duopolists. Since each of the PTAs contain a MFN provision, neither Brussels nor Washington can replay the “power play” they used to conclude the Uruguay Round: the third countries with which they have concluded PTAs may rely on the MFN provisions in those PTAs to ensure continued market access to Europe and the United States without regard to whether they continue to enjoy an MFN guarantee through WTO agreements. Proliferation of PTAs therefore poses a significant legal-political constraint on European-U.S. hegemony, a constraint that did not exist a decade ago.

* * *

Because of these shifts—the end of non-reciprocity toward the South, sustained developing country coalitions, and U.S.-and EC-centered PTA proliferation-- decision-making has become increasingly difficult in the WTO. Nothing symbolizes and illustrates this power shift[4] better than the new "Quad." In Geneva, "the Quad" no longer refers-- as it did for decades-- to the EC, Japan, Canada, and the United States, a group that effectively governed the GATT and shared fundamentally convergent views on the desirability and content of liberalization. Now "the Quad" refers to Brazil, India, the EC, and the United States, a group that has been routinely convened to advance the Doha Round but holds comparatively divergent views about what should be liberalized and who should do it.

The South, now being asked to deliver their markets to international commerce, has become an important demandeur in trade negotiations. What they want, however, is not easily squared with domestic interests in the North. The agriculture and steel industries in Europe and the United States remain well organized, well financed, and opposed to liberalization. These long-standing protectionist sectors, which have long captured government in the North, have become a key obstacle to a successful multilateral negotiation.

At the same time, the South may be unable to deliver in negotiations on key issues. If there were a deal to be struck at the WTO, it would entail a commitment by the

[4] These changes in Geneva and the ensuing stalemate do not reflect a fundamental shift in *market* power of WTO members. Some have claimed that the expanded number of developing countries in the WTO, combined with the spectacular economic growth of China and India, are shifting material bargaining power to the South. The data does not support this claim. China and India are growing, and the number of developing country members is increasing, but their markets are still comparatively small. Still, we can assume that over the next thirty years, material power at the WTO is likely to shift as Figure 1 illustrates. While predicted GDP from 2005-2035 is highly speculative, Figure 1 suggests some interesting developments: material power at the WTO will diffuse, moving toward a five-or six- power system over the next thirty years, with the United States and EC still important, but in decline, and China and India clearly rising in prominence.

South to address new behind-the-border measures. Credibly committing to such reforms, however, is difficult, given the inefficiencies in state structures in most of the developing world. In Europe and the United States, constituencies now demand that trade negotiations focus on issues such as services, investment, competition policy, labor, environment, and culture. Yet, such demands fly in the face of fundamental principles of sovereignty in the state system. Unlike border measures that invoke a political problem because they lead to factor reallocation, many of these issues implicate fundamental features of these nations such as changes in the regulatory structure and capacity of the state, the political structure of society (e.g., the power of organized labor), or the industrial structure of the economy. Rules addressing these areas are hard to establish in developing countries, where state capacity and authority structures are simply too poorly developed.

In summary, as a result of increased developing country bargaining power at the WTO, as well as divergent North-South interests and state capacity, multilateral liberalization through trade negotiations has becoming increasingly difficult. The Doha Round negotiations have been underway for six years, making them longer than any previous round other than the Uruguay Round. Yet the Doha negotiations are nowhere near as far along as the Uruguay Round negotiations were in their sixth year. From the start, the Doha negotiations have been slow-going. The Cancun Ministerial ended in deadlock in 2003. In December 2005, the Hong Kong Ministerial ended with a fig leaf of proclaimed success but with no deep substantive progress on key issues. By the summer of 2006, negotiations had collapsed and they have not been truly revived. The South will not accede to Northern demands that it reduce industrial tariffs and agricultural trade barriers; much of the South lacks the state capacity necessary to address behind-the-border issues that are of increasing interest to the North; and the North-- due largely to domestic political capture-- will not accede to Southern demands to unilaterally reduce industrial and agricultural protection and subsidization.

The Doha Round may yet be revived, but any outcome is likely to be minimalist and will not be delivered on the original timetable. Compared to the ambitions of European and U.S. trade policy makers and policy wonks before the Round was launched-- for a Round that would zero industrial tariffs, eliminate agricultural subsidies, and address environmental, labor, competition, investment, and transparency issues--even a revival of negotiations and their "successful" conclusion would yield a disappointing result.

(II) <u>The Rise of Judicial Liberalization</u>

While liberalization through negotiation has become more difficult in the last decade, liberalization (of a different quality, to be sure) has gotten easier through the litigation path. We contend that there is more litigation now than in the GATT years, that the contemporary dispute settlement system engages in more lawmaking than in the GATT years, and that WTO judicial lawmaking has a liberalizing bias.

The institutional context for change:

The rise of judicial liberalization in the GATT/WTO system, and the WTO's dispute settlement rules and processes, are best understood in the context of the GATT's dispute settlement rules and processes. The GATT was created to facilitate bargaining among participants over the regulation and liberalization of trade policy. Although concerned that nations live up to their promises, the mechanism for oversight depended upon a nation, in the name of a producer, complaining about a violation. The secretariat had neither oversight nor judicial power. Although the secretariat compiled data on trade practices starting in 1989 through the Trade Policy Review Mechanism (TPRM), the data in these reports constituted neither formal grounds for a dispute nor legal evidence of a country's trade practices. Monitoring occurred through oversight by individual contracting parties; when a complaint was filed, the Secretariat assisted in the formation of a panel. If the panel found in favor of the complainant, and the complainant did not block a consensus to adopt the panel report, then the contravening party was required to change its behavior. In the absence of a change in practice, little could be done other than sanctioning retaliation -- though that too required a consensus.

The weakness of the GATT dispute settlement procedure became increasingly apparent in the 1980s. In the early years of GATT, 1948-59, contracting parties brought a relatively few (53) legal complaints against each other. The panel procedure mentioned above was developed in these years and it was used in over half of these cases (Hudec 1999). As the number of contracting parties grew, the number of conflicts increased. Perhaps reflecting dissatisfaction with the settlement procedures, the number of formal complaints did not rise and, in fact, fell after 1963. While there were almost 60 cases that were dealt with by the dispute settlement process through 1962, only one new case was brought forward through 1970. Hudec argued the issue was legitimacy—the process was viewed as unfair (Hudec 1999). Legitimate or not, the case load increased in the 1970s to a total of 32; in the 1980s the panel process began to be regularly invoked (Hudec 1999). Of the 115 complaints filed in the 1980s, 47 led to panel reports. However, only about two-fifths of rulings for the complainant resulted in full compliance by the respondent (Busch and Reinhardt 2002, 473). Nonetheless, the increased caseload forced the Secretariat to create a separate legal division, which had the effect of encouraging even more legal complaints. As the number, visibility, and importance of cases increased so too did the number of cases in which consensus was blocked.

During the 1970s and 1980s, in response to frustration with the GATT dispute system and in the face of a growing trade deficit and the perceptions of unfair trade practices abroad, the U.S. turned to domestic law to deal with its trade problems. Specifically, a "unilateral" approach to addressing trade disputes was enacted by the U.S. Congress in the form of Section 301 of the Trade Act of 1974. Section 301 permits (and in some cases, requires) the President to impose retaliatory trade sanctions on countries engaging in practices that are "unjustifiable, discriminatory, or unfair" -- as determined by the USTR. Thus, when a foreign government blocked the GATT dispute settlement process, the U.S. government often found itself in a position of threatening unilateral trade retaliation against that government unless it agreed to change its trade practices in accordance with Washington's demands. This American approach to the settlement of trade disputes was not viewed favorably by the rest of the world.

As part of an attempt to credibly commit to the regime in the post-Cold War days and because of a belief that the U.S. was in compliance with GATT rules, the U.S. championed a toughening of the dispute settlement procedures.[5] In 1989 the U.S. had supported a new dispute settlement understanding adopted in the Midterm Review of the

[5] For more details on this argument see Goldstein and Gowa, 2003.

Uruguay Round; in the next year, the U.S. heralded an even more radical change in the rules. The underlying theme was that it was time for member nations to agree to give up their right to block a consensus in the establishment of panels, the adoption of panel reports, and retaliation. Initially aligned closely with Canada but not the other Quad members, the U.S. proposal included not only the automatic adoption of panel reports, but also created a right to appeal to a new Appellate Body whose purpose was to oversee the work of panels on questions of law. The time limits established in this process would be modeled on its own Section 301 statute. For the United States, this seemingly radical position was contingent on a crucial proviso -- that the substantive rules adopted in the Uruguay Round had to be adequately specific and reflect U.S. policy objectives.[6]

At home, increased delegation under these terms was argued to be consistent with American interests: the U.S. would remain more often in compliance with WTO rules that reflected its interests and policy objectives than would its trading partners. If the WTO's substantive rules were to its liking, and the dispute settlement procedures were both consistent with the timeline for action under Section 301 and could ultimately authorize retaliation for noncompliance, then a more legalized WTO dispute settlement system would legitimize U.S. use of its market power to pressure other countries to comply with U.S. trade policy objectives. Tellingly, the U.S. shifted to this position on dispute settlement reform at the end of 1990, at the same time that it reached agreement with the EC to impose the results of the Uruguay Round on developing countries via the "single undertaking." Few nations agreed with the U.S. analysis of who would end up in front of panels. But curbing U.S. unilateralism was one of the most salient elements in both Japan’s and the EC’s publicly stated interest in the Round and both endorsed the reforms.

In the end, the new procedures occupied 35 pages of text and an elaborate accompanying description. The process is far more complex and precise than in the past and covers all areas of WTO agreements, including Section 301 actions by the United States. The DSU is far more obligatory, automatic, and apolitical than the GATT rules. The effect of the change -- a vast increase in use of the DSU -- was far broader than was

[6] This description of the U.S. position in 1990 is documented in USTR, Dispute Settlement, U.S. Objectives for Brussels, in The U.S. Delegation Briefing Book for the Brussels Ministerial, December 1990 (on file with the authors).

anticipated by most. While 535 dispute settlement complaints were filed in the 46-year period of the GATT system, 269 complaints were filed in the first eight years alone of the WTO system.[7]

(III) **The Impact of Regulatory Change**

The dispute settlement change meant that two substantive shifts occurred in the WTO judicial system. First, judicial action became more automatic. A consensus is now required to *block* the formation of a panel, adoption of a report, or an authorization of retaliation for continued non-compliance -- a reversal of the former rule that required a consensus to move through each of these stages. Of course, petitioners would not agree to block establishment of a panel they are demanding, and prevailing parties would not block the adoption of favorable panel reports.

Second, the reform led to the creation of a judicial body to which nations could appeal panel reports. The Appellate Body's mandate is formally limited to the review of legal findings made by panels, given the facts established by the panel. The Appellate Body has seven members, chosen by the Members at large, and appeals are heard by a subset of three members.

The automaticity of the new system, and the promise that it has held for aggrieved members, has led to an increased caseload for the WTO dispute settlement system, compared to the GATT dispute settlement system. Moreover, because of automaticity, there were more dispositive reports (i.e., adopted panel reports in cases where there was no appeal; adopted Appellate Body reports in all other cases) issued in the first six years of the WTO system than in the last twenty years of the GATT system (Busch and Reinhardt 2003; Steinberg 2004). And there are far more parties to WTO disputes than to GATT disputes. In the GATT era, it was rare for a case to feature more than one complainant. In contrast, in the WTO era, in nearly half of all cases there are multiple complainants or interested third parties. Not only have caseloads increased, so has the number of parties involved in each dispute.

[7] Data for the 1995-2003 period is from Leitner and Lester 2004. Data from the 1948-95 period is from Busch and Reinhardt 2002. These include complaints that ended prior to a panel decision and those that went on to be decided by a panel and adopted by the members.

The Emergence of Judicial Lawmaking:

Many scholars have suggested that judges may behave strategically and favor increasing their authority (Burley and Mattli 1993; Ferejohn and Weingast 1992; Voeten 2007), yet few Uruguay Round negotiators anticipated or intended the Appellate Body to engage in lawmaking.[8] The switch to automatic, binding dispute resolution, and the establishment of the Appellate Body were seen by the United States as an opportunity to foster implementation of and compliance with the deals struck in the legislative process -- even if those deals were not optimally efficient and even if they were not considered equitable. The dispute settlement process was to fulfill that purpose by offering a neutral judicial process to enforce WTO agreements the substance of which was largely favored by the United States. Most U.S. policy-makers at the time expected WTO dispute settlement to enforce the WTO "contract;" they did not expect or accurately anticipate that the Appellate Body would make law.

As in domestic legal systems, rules and principles guiding the interpretation of public international law permitted the Appellate Body to take a range of interpretive stances: at one extreme, a restrained interpretive stance that is highly deferential to the express consent of states; at the other extreme, an expansive interpretive stance that is less deferential to state consent, favors dynamic interpretation of treaty provisions, and expands upon terms and gaps. Largely in the interests of completeness, coherence, and internal consistency of WTO law, the Appellate Body chose a more expansive stance both on questions of whether to interpret and on the method used for interpretation. The resulting judicial decisions have created an expansive body of new law.

WTO judicial law-making has two dimensions: filling gaps and clarifying ambiguities. Gap-filling refers to judicial law-making on a question for which there is no

[8] Interviews with A. Jane Bradley, former chief U.S. dispute settlement negotiator and Assistant USTR for Enforcement (March 2007) and with Kenneth Freiberg, USTR Deputy Gen. Counsel (March 2007), support this conclusion. A handful of lawyers in the USTR's General Counsel's office were concerned about judicial lawmaking, but those at the political level in both Washington and Brussels were persuaded by the clarity of the WTO agreements and the WTO DSU Art. 3.2 and 19.2 mandates that neither panels nor the Appellate Body could "add to nor diminish the rights and obligations provided in the covered agreements." U.S. Senator Bob Dole was concerned enough about judicial lawmaking that he proposed establishment of a commission to review the decisions and behavior of the Appellate Body, but only twelve co-sponsors joined him in support of the proposal and it never passed the Senate.

legal text directly on point, whereas ambiguity clarification refers to judicial law-making on a question for which there is legal text but that text needs clarification.[9]

First, the DSU's silence on many procedural questions has been seen by some as an invitation to the Appellate Body to make procedural rules. In some cases, the Appellate Body has created law that fills procedural gaps in WTO agreements, even though the existence of the gap has resulted from sharp disagreement among Members about how to fill it. For example, in *United States - Import Prohibition of Certain Shrimp and Shrimp Products* (*U.S. - Shrimp-Turtle) (2000)*, the Appellate Body decided -- without clear guidance from WTO agreements -- that dispute settlement panels could consider *amicus curiae* briefs submitted by non-state actors. In so ruling, the Appellate Body relied on general language in DSU Article 13, which provides that panels have a right to seek information and technical advice from any individual or body that it deems appropriate. Regardless of the merits on the question, the Appellate Body's interpretation of Article 13 was made in the context of several years of North-South deadlock on the question of whether to permit *amicus* briefs: few developing countries would have consented to an agreement with that outcome, yet the Appellate Body chose to interpret the DSU as supporting it.

Similarly, in *European Communities - Regime for the Importation, Sale and Distribution of Bananas* (*EC – Bananas)(1997)*, the Appellate Body established that private lawyers may represent Members in its oral proceedings, despite EC and U.S. opposition on grounds that the practice from the earliest years of the GATT was to permit presentations in dispute settlement proceedings exclusively by government lawyers or government trade experts. The Appellate Body acted at odds with nearly fifty years of GATT practice, reasoning that nothing in WTO agreements, customary international law, or the "prevailing practice of international tribunals ... prevents a WTO Member from determining the composition of its delegation in Appellate Body proceedings." At the panel stage, this practice of permitting participation by non-government lawyers was subsequently adopted in *Indonesia - Certain Measures Affecting the Automobile Industry* (*Indonesia - Autos) (1998).*

[9] Ultimately, the distinction between gap-filling and ambiguity clarification may be fragile, but the distinction is respected here out of convention. See generally Hart 1961.

Second, the WTO Appellate Body has engaged repeatedly in a form of law-making by which it has given specific meaning to ambiguous treaty language. Such clarifications may cause a negative political reaction by Members or non-governmental stakeholders that engaged in behavior that was within a range of possible meanings, given the ambiguity. For example, in *U.S. - Shrimp-Turtle*, the Appellate Body decided whether the United States could rely on GATT Article XX(g) to ban the importation of certain shrimp and shrimp products from Members that did not maintain laws that guaranteed particular methods of protecting endangered sea turtles in the process of shrimp fishing. GATT Article XX(g) excepts certain measures from the GATT's affirmative obligations if they are necessary for the "conservation of exhaustible natural resources," but the provision is ambiguous through silence on the question of whether such exhaustible natural resources must be located within the jurisdiction of the country invoking the exception. Earlier decisions suggesting that they must catalyzed enormous debate by the members. The Appellate Body offered a dynamic interpretation of the conditions under which the GATT Article XX(g) exception for conservation of exhaustible natural resources could be invoked, stating that it must be read "in light of contemporary concerns of the community of nations about the protection and conservation of the environment." After concluding that the measures in question fell within the meaning of Article XX(g), the Appellate Body interpreted the chapeau to Article XX and established at least five specific factors that would apply in considering whether a measure contravenes the terms of the chapeau. Some of the factors had no textual lineage (e.g., whether the respondent's actions have an "intended and coercive effect on the specific policy decisions of other members"). In short, the Appellate Body ruling provided an approach to balancing trade-environment issues, despite WTO Members having been deadlocked for a decade about how to achieve balance on the question.

Third, in a number of instances, the Appellate Body has given precise and narrow meaning to language that was intentionally left vague by negotiators, either because they could not agree on more specific language, or in order to permit a range of alternative behaviors or national practices. For example, in three decisions, *United States - Safeguard Measures on Imports of Fresh, Chilled or Frozen Lamb Meat from New*

Zealand and Australia, (2001) United States - Definitive Safeguard Measures on Imports of Wheat Gluten from the European Communities (2000), and United States - Definitive Safeguard Measures on Imports of Circular Welded Carbon Quality Line Pipe from Korea, (2002), the Appellate Body fleshed out the causation analysis to be used in safeguards cases, which Uruguay Round negotiators intentionally left ambiguous.[10] In the *Lamb Meat* case, for example, based on the obligation not to attribute injury from other causes to imports that were the subject of a safeguards investigation, the Appellate Body established an affirmative requirement that national authorities analyze not only the nature but also the "extent" of other causes. A similar approach was taken in the anti-dumping context in *United States - Antidumping Measures on Certain Hot-Rolled Steel Products from Japan* (*U.S. - Japan Hot-Rolled Steel)(2001*). The U.S. government and commentators have identified several other cases in which the Appellate Body or dispute settlement panels have given a specific and narrow interpretation of language in WTO agreements that was intended by at least some of its negotiators to be ambiguous and to permit a range of national practices (U.S. Secretary of Commerce 2002, Tarullo 2003, Barfield 2001). Decisions like these might enhance efficiency (Sykes 1991), but they are certain to engender negative political reactions in countries that intended to consent to broader interpretations.

Finally, a conflict between GATT/WTO texts (or between text and GATT practice) may create an ambiguity and in a handful of cases, the Appellate Body has read language across GATT/WTO agreements cumulatively in a way that has generated an expansive set of legal obligations. Perhaps most controversially, in *U.S. - Lambmeat* and *Argentina - Safeguard Measures on Imports of Footwear, (1999),* the Appellate Body ruled that national authorities imposing a safeguards measure must demonstrate the existence of "unforeseen developments." In the 1952 *U.S. - Hatters' Fur* case, a GATT Working Party had agreed that the application of Article XIX safeguards measures could be based on an argument that an unexpected degree of change in consumer tastes that increased imports constituted demonstration of "unforeseen developments." Given that

[10] In the Uruguay Round negotiations, U.S. negotiators had refused to agree to a test that would require national authorities to quantify the relative effects of imports and other factors on domestic industry. In so refusing, the U.S. negotiators intended to enable the ITC to continue using its qualitative approach to analysis of the "substantial cause" question in safeguards cases (Reif 2002).

implicitly broad interpretation of the phrase, which would seem to allow almost any increase in imports to constitute "unforeseen developments," subsequent GATT panels did not require national authorities to demonstrate "unforeseen developments" prior to imposing safeguards measures. Moreover, the WTO Safeguards Agreement makes no reference to a requirement to demonstrate "unforeseen developments," and the negotiators expressly considered and rejected inclusion of any such requirement. The cumulation of GATT practice, relevant texts, and negotiating history created an ambiguity over whether "unforeseen developments" must be demonstrated in safeguards cases. Focusing on GATT Article XIX:1(a), the Appellate Body read all of the relevant GATT/WTO law and practice cumulatively in a way that led to the conclusion that a demonstration of "unforeseen developments" must be shown if a safeguards measure is to be applied.

While there is no doubt that the WTO Appellate Body is making law, we do not claim that it has, on balance, been irresponsibly "activist."[11] All courts make law to varying degrees. The Appellate Body has not shied away from lawmaking, but it has at times restrained itself, demonstrating some sensitivity to politics. For example, it has sometimes invoked the doctrine of "judicial economy" to limit the extent to which it interprets WTO agreements in any particular case.[12] This measure of self-restraint begs the question: How expansive is WTO judicial lawmaking?

The Expansiveness of Judicial Lawmaking: the GATT and WTO Compared:

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[11] "Activism" is a term subject to alternative definitions and normative assessments. For example, compare textualist with dynamic approaches to activist statutory interpretation. *E.g.* Frank H. Easterbrook, *Statutes' Domains*, 50 U. CHI. L. REV. 533, 547 (1983); William N. Eskridge, Jr., *Politics Without Romance: Implications of Public Choice Theory for Statutory Interpretation*, 74 VA. L. REV. 275 (1988); Karen M. Gebbia-Pinetti, *Statutory Interpretation, Democratic Legitimacy and Legal System Values*, 21 SETON HALL LEGIS. J. 233, 281 (1997); John F. Manning, *Textualism as a Nondelegation Doctrine*, 97 COLUM. L. REV. 673, 685 (1997); Nicholas S. Zeppos, *The Use of Authority in Statutory Interpretation: An Empirical Analysis*, 70 TEX. L. REV. 1073, 1078–79 (1992). Debates over WTO activism usually consider Appellate Body holdings that domestic measures contravene WTO obligations, or whether the Appellate Body has remained true to some posited, deduced, or constructed intent of those who negotiated a substantive provision of a WTO agreement. Most of those characterizing WTO dispute settlement as "activist" do so pejoratively.

[12] See, e.g., European Communities–Measures Affecting the Importation of Certain Poultry Products, WTO Doc. WT/DS69/AB/R, ¶135 (July 23, 1998); United States–Measure Affecting Imports of Woven Shirts and Blouses from India, WTO Doc. WT/DS33/AB/R, §VI (Apr. 25, 1997).

Is WTO lawmaking more expensive than lawmaking in the GATT era? Some commentators have attempted to quantify the extent of judicial lawmaking (often referred to as "activism") in municipal or comparative contexts (Cannon 1982; Lijphart 1999). Virtually every such effort measures the rate at which constitutional courts strike down laws. Empirically, analysis of GATT and WTO dispute settlement reports reveals no statistically significant difference between the two systems in the per case likelihood that national laws will be deemed inconsistent with GATT/WTO obligations (Steinberg 2004). However, these data imply that the annual volume of such lawmaking may have increased, since there are many more dispositive WTO reports per year than adopted panel reports per year in the GATT era.

Comparing the extent of lawmaking in the WTO and GATT eras by using such a measure is of limited value in explaining how the GATT/WTO legal system has changed. Conceptually, the nature of judicial action may change across several dimensions – not just the dimension measured by lawmaking – as political or constitutional context changes.

Evaluating the expansiveness of judicial lawmaking demands a multidimensional analysis that focuses on the rate and scope of judicial gap filling and ambiguity clarification, factored by the volume of dispositive dispute settlement reports.[13] The rate of judicial lawmaking refers to the proportion of dispute settlement reports in which ambiguity is clarified or gaps are filled. The scope of judicial lawmaking refers to the extent to which ambiguity is clarified or a gap is filled. The volume of dispute settlement reports refers to the number of dispositive reports adopted annually by the Dispute Settlement Body (DSB).

Rigorous quantitative comparison of the expansiveness of GATT and WTO judicial lawmaking is difficult, because measuring the rate and scope of ambiguity clarification or gap filling by a particular court entail highly qualitative judgments.

[13] See Robert Keohane, Andrew Moravcsik, and Anne-Marie Slaughter in Keohane et al. 2000.

Nonetheless, there are good reasons to believe that judicial lawmaking is more expansive in the WTO than in the GATT era. As discussed above, GATT panel reports were aimed at the diplomatic settlement of disputes, whereas WTO dispute settlement serves an essentially adjudicative function. GATT panel reports had no legal effect unless they were adopted by consensus; in effect, no law could be made without the consent of the Contracting Parties, whereas WTO dispute settlement reports are adopted by negative consensus. As a result, GATT judicial lawmaking could not be expected to have been as bold and far-reaching in scope as judicial lawmaking in the WTO. Moreover, even if no change had occurred in the rate of scope of judicial lawmaking since the GATT era, judicial lawmaking would still be more expansive in the WTO system because of the increased dispute settlement caseload described above.

Given the highly qualitative nature of any comparative assessment of the expansiveness of judicial lawmaking, the consequent contestability of any individual effort to make such an assessment, the potential selection bias inherent in the body of cases concluded by each of the two dispute settlement systems, and variance in the form of GATT dispute settlement over time (i.e., its increasing legalization), it is more useful to consider a few indicators of change in the expansiveness of judicial lawmaking than to offer any single commentator's reportedly quantitative or qualitative assessment of change.

Several indicators suggest that judicial lawmaking is more expansive in the WTO than in the GATT. Compare, for example, discussions about judicial lawmaking by DSU negotiators in the GATT Uruguay Round to discussions by DSU negotiators in the Doha Round. Analysis of publicly available notes by the secretariat concerning the Uruguay Round Negotiating Group on Dispute Settlement indicates no instance in which a negotiator suggested that GATT dispute settlement panels were activist or engaged in expansive lawmaking.[14] While the Uruguay Round preparatory materials are incomplete, the leading secondary history of the Uruguay Round DSU negotiations nowhere mentioned any discussion of activism or lawmaking by GATT panels (Croome 1995).

[14] Judicial lawmaking was raised several times in the Uruguay Round dispute settlement negotiations, but in all those instances participants were expressing a preference that prospective changes in the dispute settlement system should not create, by constructive interpretation, obligations that were not established in the texts of GATT/WTO agreements. (GATT Secretariat 1987; GATT Secretariat 1998).

Finally, lawyers from the Office of the United States Trade Representative (USTR) identified only four GATT panel reports that were criticized by contracting parties as instances of overly broad lawmaking or inappropriate interpretation.[15]

In contrast, analysis of publicly available official documents of the Doha Round Negotiating Group on Dispute Settlement, which has convened in special sessions of the DSB, indicates that in just the first 18 months of negotiations – by June 2003 – concern about instances of or proposed solutions to judicial law-making by WTO panels or the Appellate Body were raised 77 times by representatives of 55 members (including the EC and the United States), focusing on at least ten dispositive WTO dispute settlement reports adopted in the WTO's first eight years. Moreover, confidential notes on meetings of the DSU Reform Group, in which ambassadors representing approximately ten members have met regularly for informal discussions of concerns about the operation of the DSU, reveal that judicial law-making was considered at almost every meeting during the period for which the notes are available.

Consider also journal articles on the subject. Of 110 selected U.S. and Canadian law journal articles on GATT dispute settlement published from 1982-1994 (the last year of the GATT system), only two mention cases in which controversial, expansive, or activist judicial law-making might have taken place. In contrast, at least 51 articles published in similarly selected U.S. and Canadian law journals in the first eight years of the WTO discuss controversial, expansive, or activist judicial law-making for cases in the WTO period (Steinberg 2004).

More broadly, we note that the emergence of a public policy debate over judicial activism in the WTO, a debate that simply did not exist in the GATT years. Several prominent commentators,[16] lawyers,[17] leaders of non-governmental organizations,[18] and

[15] Telephone interviews with A. Jane Bradley and Kenneth Freiberg, January 2003, described in Steinberg 2004b, 256, n. 68.

[16] *See, e.g.*, Barfield 2001; Raustiala 2000; Tarullo 2002.

[17] *See, e.g.*, Ragosta 2003.

[18] *See, e.g.*, Wallach 2000.

politicians from the United States[19] and abroad[20] have suggested that the WTO Appellate Body is engaging in judicial activism.

Liberalization Through WTO Dispute Settlement?

In most cases, Appellate Body interpretations have favored more trade openness. In all cases, complainants advance interpretations of WTO agreements that challenge a respondent's trade barrier, and respondents argue for interpretations that would permit maintenance of the barrier. For WTO cases initiated before 2001, 89 percent of the 152 dispositive reports held that at least one of national measures at issue was WTO-inconsistent (Busch and Reinhardt 2003). Qualitative assessments of Appellate Body decisions, such as those by Dan Tarullo, have also shown a liberalizing bias (Tarullo 2002).

Some might hypothesize that the Appellate Body nonetheless favors protectionist interpretations in cases involving measures putatively adopted for reasons related to consumer or environmental protection. But several decisions run contrary to that claim: for example, in the *EC-Beef Hormones* case, and in the more recent *EC-GMO* case, the WTO Appellate Body has shown little tolerance for interpretations favoring closure, even though those cases raised politically sensitive social concerns. Even in cases where the Appellate Body has ultimately permitted social measures to serve as a barrier to trade, it has made law that restricts the conditions under which such measures may be maintained or applied, as in the *US- Shrimp-Turtle* case analyzed above. We do not argue that the Appellate Body always favors liberalization, but its decisions do seem biased toward liberalization and its opinions tend to suggest a view of the WTO more as an instrument

[19] Senator Max Baucus stated that WTO panels are "making up rules that the U.S. never negotiated, that Congress never approved, and I suspect, that Congress would never approve." *US DSU Proposal Receives Mixed Reactions*, BRIDGES WKLY. TRADE NEWS DIG., Dec. 20, 2002, at 10, *at* <http://www.ictsd.org/weekly/02-12-20/wtoinbrief.htm> [hereinafter Baucus Statement].

[20] Negotiations on the Dispute Settlement Understanding, Proposal of the Africa Group in the WTO ¶2 (Oct. 2002) (on file with author) [hereinafter Proposal of the Africa Group].

of liberalization than a reflection of a contractual balance between liberalization and protection captured by the concept of embedded liberalism (Haas 1982).

(IV) Away From Capture: Why Judicial Liberalization Works

WTO judicial liberalization may be as, or even more, efficient at reaching the stated goal of the WTO to liberalize trade than the traditional trade rounds. Judicial decision-making has successfully freed states from capture by entrenched import-competing interests in a way that negotiated liberalization was not able to accomplish. This regulatory shift explains the strikingly high rate of compliance with judicial lawmaking.

Since its creation, in only one out of over twenty dispositive WTO cases is a losing party held to have failed to comply within a “reasonable period.” This 95 percent rate of compliance with judicial decisions would be respectable in most national legal systems. That it persists in an international legal context, which many describe as “anarchic,” may be surprising. This compliance rate is particularly impressive, given that compliance with WTO dispute settlement decisions typically involves political defeat for historically powerful and intransigent protectionist sectors that for decades have captured domestic trade policymaking. Why does the WTO dispute settlement system enjoy such a high compliance rate?

As a matter of international law, there is a legal obligation to comply with adopted WTO Appellate Body decisions (Jackson 1997). But as a matter of domestic law, few if any national legal systems give direct effect to Appellate Body decisions. As a matter of domestic law, sovereignty has not been “delegated” to the WTO Appellate Body. Therefore, behaviorally, compliance is a domestic political decision.

The essence of the mechanics by which the dispute settlement system enjoys such a high compliance rate is rooted in decentralized enforcement—a legitimized retaliatory threat that reconfigures domestic politics in the contravening country. At the interstate level of analysis, when ruled against, a Member is expected to comply within a "reasonable period of time" (which is determined by a WTO panel). If not, the adversely affected complainant can retaliate. Retaliation takes the form of raising tariffs on goods originating in the territory of the contravening country to a level that is intended to have the effect of eliminating demand for the imports in proportion to the adverse effect of the contravening measures.

At the domestic politics level, the potency of this mechanism becomes clear. The dispute settlement system provides national leaders with a way to get around domestic pressures to keep the market closed. The potential of retaliation is an important means to motivate exporters who will be hurt by the sanction. Since countries publish a list of products that will be effected by the sanction (in the U.S. case, the government publishes a proposed retaliation list in the Federal Register thirty days prior to the effective date of retaliation) this has the effect of pitting those politically powerful export-oriented producers against the industry that champions the contravening measures. If targeted smartly, the proposed retaliation list mobilizes sufficient political muscle within the contravening country to result in WTO-consistent reform. In this way, the DSU works in conjunction with domestic laws, regulations, and politics to foster compliance with the legislative outcomes that are codified in the WTO agreements (Goldstein and Martin 2000).

The use of judicial action to open markets and the acquiescence of the US to appellate decisions does not imply that the United States favors the extent of judicial liberalization currently taking place at the WTO. As we argued above, there is little evidence in the negotiating history of the DSU that suggests that the move to legalization of GATT/WTO dispute resolution was intended or expected to lead to expansive judicial liberalization. Then why hasn't judicial liberalization been checked?

In effect, the expansive interpretive stance by the Appellate Body *has* faced *some* limits. For example, powerful members particularly the EC and the United States, have had a *de facto* veto over the appointment of Appellate Body members: in the WTO's early years, these powerful members engage in a comparatively cursory review of Appellate Body nominees; in more recent years, as the Appellate Body's capacity to make law became apparent, the United States began engaging in a thorough review and interview of Appellate Body nominees, blocking the appointment of some nominees who were seen as too activist. Similarly, members have not been shy about complaining when the Appellate Body engages in lawmaking they dislike, and proposals by powerful members to rewrite parts of the DSU in the Doha Round may have had a sobering effect on the Appellate Body. To some extent, agent slack has been limited.

Nonetheless, developing countries have not joined efforts to curb judicial liberalization at the WTO. While many developing country representatives have complained about judicial "activism" by the Appellate Body, their bigger complaint appears to focus on the relative incapacity of developing countries to fully avail themselves of the dispute settlement system. As a formal matter, developing countries have as much access to the WTO dispute settlement system as developed countries do. Yet in practice, there is emerging evidence that developing countries may use dispute settlement procedures significantly less often than developed countries. The explanations for this difference are a topic of contemporary debate, but they include the lack of resources in developing countries to spend on WTO litigation (i.e., large bills from lawyers and econometricians); the structure of interest organization in developing countries, where collective action problems may have not been overcome; pressure from Brussels and Washington to refrain from bringing cases; and the lack of legal and economic expertise and sophistication in developing countries (Brown and Hoekman 2005; Guzman and Simmons 2005). Despite these problems, some developing countries, such as Brazil and India, have not been shy about taking developed countries, such as the EC and United States to dispute settlement. In so far as more sophisticated developing countries that may be on the edge of development choose to litigate, they may act as proxies for the developing world, knocking down protectionism in the North.

Perhaps that is why the developing countries have blocked U.S. efforts to reign in WTO judicial lawmaking. In the Doha Round, the United States has proposed several judicial reforms that are intended to curb Appellate Body lawmaking. The central U.S. proposal in this regard would permit the parties to a dispute to agree to excise from draft Appellate Body decisions language they find objectionable. Such a rule would (and is intended to) enable the parties to a dispute to have greater control over the content of Appellate Body opinions. It is also obvious that under that rule a powerful respondent (such as the United States) could offer a petitioner a side-payment (or compliant behavior) in order to eliminate disagreeable acts of Appellate Body lawmaking. Despite their own complaints about Appellate Body activism, the developing countries have blocked progress on this proposal and others on the ground that they would diminish the Appellate Body's independence.

More broadly, a lack of consensus on all aspects of ministerial decision-making helps explain the lack of oversight of the judiciary. Legislative deadlock in the WTO has diminished the ability to check the Appellate Body.

Conclusions: Consequences of Judicial Lawmaking as the Locus of WTO Liberalization

No one at the time of the signing of the WTO agreement predicted that the organization would suffer from legislative gridlock. Similarly, there was scant indication that the Appellate Body would be a force for economic liberalization. In fact, the EC and United States had considered and rejected alternative legislative decision-making rules, such as trade-weighted voting, because in the early 1990s they saw no challenge to their joint management of the regime. And as suggested above, when U.S. negotiators supported a shift from the GATT to the WTO dispute settlement rules, they expected the new dispute settlement system to neutrally enforce rules that were favored by the United States and Europe – not judicial liberalization. The rise of a developing nation coalition bloc, like the rise of judicial liberalization at the WTO, was the result of fundamentally unanticipated institutional and political developments. And the lack of consensus among the ministers has led to an absence of oversight of their judicial agent. In short, legislative deadlock led to a shift in regulatory authority of the judicial branch of the WTO.

Though unanticipated, legislative stalemate and judicial lawmaking may solve a dilemma facing free trade oriented leaders in the advanced economies. Trade liberalization today is more difficult than in any earlier period. With more information in hand, groups that will suffer from a change in trade policy are more knowledgeable and better organized than ever before, making it difficult for elected leaders to support WTO market-opening efforts. More than ever, negotiated liberalization is difficult and export interests do not necessarily hold sway over powerful private groups unwilling to face international competition. The WTO dispute settlement system offers an alternative to negotiated liberalization with a potential for liberalizing sub-sectors that could not be opened through traditional trade negotiations. While big bundled deals gained majority support in the United States and elsewhere during the GATT years, judicial action has come to be a more salient and effective means of defeating recalcitrant protectionism. In trade negotiations, U.S. steel, sugar, cotton, apparel, and other inefficient producers have succeeded for a half century in assuring their continued protection: facing certain devastating losses from liberalization, they have remained united in successfully keeping themselves off the bargaining table, capturing U.S. trade policy. Negotiated liberalization of these sectors has been stuck in the mud.

The WTO dispute settlement process turns that politics on its head. By making decisions individually, the courts undermine the ability of groups to bundle their interests with that of other groups. At the end of the dispute settlement process, the threat of retaliation pits one of the offending protectionist sub-sectors against a large number of export-oriented interests. If retaliation occurs, certain loss will now befall the exporters, motivating them to support ending the protection under challenge. In the dispute settlement context, the export-oriented producers who in the legislative context merely had a possible gain are now threatened with a clear and credible loss, motivating them to act decisively against protection. This asymmetry – many exporters against a single import-competing group – creates the political space that pushes liberalization forward. And over the longer term, those sectors that are liberalized by judicial action will adjust and often die, eliminating them from a potential coalition that might otherwise emerge to oppose judicial liberalization (Hatahway 1998). Judicial liberalization is currently a crucial piece of the contemporary WTO liberalization story.

This important role for the WTO dispute settlement system is reminiscent of the crucial liberalizing role played by the ECJ in the 1960's through the late 1980's – until the Single European Act. In that period, the Council was paralyzed by the Luxemburg Compromise, which effectively required unanimity for any important action. The ECJ's exercise in "negative liberalization," striking down national protectionist measures in such famous cases as the *Rheinheitsgebot* and *Cassis de Dijon* cases, is credited with being the main engine of internal market liberalization in the period (Burley and Mattli 1993; Garrett et al. 1998; Alter 2000). Of course, the ECJ's role is distinguishable from that of the WTO Appellate Body in the contemporary period: perhaps most significantly, the ECJ established direct effects and unqualified supremacy of its decisions in member-state legal systems, whereas the Appellate Body has to rely on the political mechanisms described above for compliance.

None of this suggests that judicial liberalization is a perfect substitute for negotiated liberalization. Judicial liberalization is limited in its pace; it liberalizes one product or sub-sector at a time. It is limited in its depth; for example, litigation usually cannot reduce tariffs. And it is limited in its breadth; it is hard to see how the Appellate Body could comprehensively address the newer issues of integration- environment, labor, competition law, and investment – that many from the United States and Europe would like to see on the WTO's legislative agenda. Legal language in WTO instruments offers some discursive constraint on the Appellate Body's establishment of new, comprehensive rules on these topics.

And we are not predicting a permanent demise of negotiated liberalization at the WTO. As countries develop, some of their interests are likely to change and may converge with those of the EC and United States. Moreover, as judicial liberalization peels off and defeats protectionist sectors, it may be easier to agree to negotiate liberalization. In this way, judicial liberalization may feed back onto negotiated liberalization.

Nonetheless, the dispute settlement process will remain a key feature of WTO liberalization for years to come. Ultimately, agent slack for a judiciary is inversely related to the possibility that the legislature can correct it. In the WTO, the capacity to legislate is diminishing. The Doha Round collapsed and although it has been formally revived little progress has been achieved. Over time, the GATT/WTO system has evolved from a hegemonic structure, to a hegemonic duopoly, to tri-polarity (the United States, EC, and developing countries) today – and over the next few decades it seems headed for multi-polarity with a divergence of interests of key members. This would suggest increasing agent slack for the WTO's judicial system and the persistence of judicial liberalization.

Rhs/documents/articles/Goldstein and Steinberg/Oxford/ Rise of Judicial Liberalization (G-S re-edited 10.22.07)

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