CHAPTER 12

INTERNATIONAL COOPERATION IN ECONOMIC RELATIONS

12.1. Introduction

It is no exaggeration to say that **free trade** has become one of the most important questions of the 21st century. Recent events have opened a new chapter in international economic relations, and these changes made it necessary to rethink some of our fundamental concepts such as global governance, state sovereignty and regulatory autonomy.[1]

> Free trade means exchange of goods and services free of customs duties and quantitative restrictions.

The most recent period of world trade created a very **special political and social context** for the tree trade 'boom' we experience today.

First, the failure of the most recent, Doha Round of WTO negotiations suggests that, in global trade, **multilateralism reached its limits** and pushed pro-free-trade states towards bilateralism (or restricted multilateralism). Furthermore, while some states reverted to protectionism, others considered free trade as a way out of the current economic crises.

> Protectionism is the umbrella term of state measures and efforts that aim to protect the local economy from the pressure of foreign competition. It is used to designate state measures which are seemingly motivated by public interest goals, but their actual purpose is the protection of the local economy.

This resulted in a new generation of free trade agreements, like the Transatlantic Trade and Investment Partnership (TTIP), the Trans-Pacific Partnership (TPP), which has been reinstated by the parties in March 2018 under the name Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) due to the USA leaving the cooperation. We could also mention the EU-Canada Comprehensive Economic and Trade Agreement (CETA)[2], the EU-Japan Economic Partnership Agreement (JEFTA) finalized in 2017 December[3], and the Trade in Services Agreement (TiSA), a multilateral agreement of restricted geographical scope.

Second, it appears that the global system fulfilled its mission by minimizing traditional trade restrictions[4] and the **focus of world trade shifted** from traditional trade restraints to seemingly non-discriminatory regulatory restraints, and was extended to other subjects of trade, such as services,

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[1] The erosion of sovereignty (as it is traditionally understood) has of course started long ago. See: Jackson 2006, 57-78.

[2] CETA came into force on 21 September 2017. Council Decision (EU) 2017/38 of 28 October 2016 on the provisional application of the Comprehensive Economic and Trade Agreement (CETA) between Canada, of the one part, and the European Union and its Member States, of the other part. OJ L 11, 14.1.2017, p. 1080-1081. See Press Release: EU-Canada trade agreement enters into force (20 September 2017), available at http://trade.ec.europa.eu/doclib/press/index.cfm?id=1723

[3] JEFTA is currently waiting on the approval of the European Parliament and the member states. Press Release: EU and Japan finalise Economic Partnership Agreement (8 December 2017), available at http://trade.ec.europa.eu/doclib/press/index.cfm?id=1767

[4] See for example Factsheet on Trade in goods and customs duties in TTIP, available at http://trade.ec.europa.eu/doclib/docs/2015/january/tradoc_152998.1%20Trade%20in%20goods%20and%20customs%20tariffs.pdf

technology and capital. It shall be taken into account that in the last period the social role of regulation strengthened extraordinarily and, today, its significance in the market is incomparably higher than it was at the age when the principles of the law of economic relations were worked out.

This chapter examines two questions. On one hand, it showcases the results of the cooperation arising from this international, global trade regime. On the other, it also examines the most important aspects of new generation free trade agreements.

> The primary goal of traditional free trade agreements was to eradicate abolish quantitative restrictions and customs duties (tariffs) between the MS. In addition to this, new generation free trade agreements aim at securing the 'smooth course' of trade through ironing out different regulatory obstacles. In both cases, MS reserve all freedom to shape their trade policy regarding third countries. In contrast, in a customs union, the MS not only abolish customs duties and quantitative restrictions between each other, but at the same time they apply unified tariffs and quantitative restrictions in relation to third countries.

12.2. The Comprehensive Liberalization of World Trade

The contemporary history of world trade was opened by the conclusion of 1947 General Agreement on Tariffs and Trade (**GATT '47**) and was consummated by the creation of the **World Trade Organization in 1994** (WTO). Revolutionary changes took place in world trade during this period. Initially, GATT '47 constituted a forum of cooperation for market-based economies and was rejected by Socialist countries.[5] The collapse of Communism considerably expanded the club's membership, and in essence, the WTO's rules became universally effective. With the accession of China and Russia, the WTO became the one and only global framework for trade. In contrast to GATT '47, founded by 23 countries, WTO currently has more than 160 members. With the accession of China in 2001 and Russia in 2012, the WTO **became a truly universal trade organization**: its member countries account for 96.4% of the global GDP.

WTO law considerably limits the use of traditional trade restrictions. It virtually prohibits all kinds of **quantitative restrictions** (quotas) and significantly restricts tariffs. GATT '47 prohibited quantitative restrictions at large[6] and forced MS to transform their quantitative restrictions into tariffs (tarification). In addition, it created a system under which – regarding their own tariffs – MS accepted 'tariff-bindings' in the form of **bound tariffs**.

The era hallmarked by GATT '47 resulted in a **remarkable tariff reduction**. The pre-1947 20-30% average tariff rate[7] fell considerably. The 2007 WTO World Trade report concluded that in developed countries the average duty rate of industrial products fell to less than 4%.[8] UNCTAD's 2013

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[5] With the notable exception of Czechoslovakia and Cuba, which were founding members and remained a member after the Communists seized power. China was also a founding member but subsequently withdrew from GATT after the Communists took power. Interestingly, it was not the People's Republic of China but the Republic of China governed by the Kuo Min Tang, having fled to Taiwan, which notified the withdrawal as the entity occupying China's seat at the relevant time. Hsiao 1994, 433-434.

[6] Article XI GATT

[7] WTO (2007)*World Trade Report: Six Decades of Multilateral Cooperation*, *What Have we Learnt*? Geneva: WTO. p. 207. available at https://www.wto.org/english/res_e/booksp_e/anrep_e/world_trade_report07_e.pdf. Cf. Bown–Irwin 2015 (Finding that the average tariff level in 1947 was about 22%).

[8] WTO (2007)*World Trade Report: Six Decades of Multilateral Cooperation*, *What Have we Learnt*?Geneva: WTO. p. XXXI. After the Uruguay Round, the weighted bound tariff average of the United States, Japan and EU (at that time having 12 Member States) was 3.1%, with the US having 3.5%, Japan 1.7% and the EU 3.6%. Ibid. p. 209.

Key Statistics and Trends in Trade Policy reported that in 2012 the average applied tariff was 1% in developed countries and between 4%-10% in developing countries.[9] As for the distribution of tariff burdens, it reported that approximately 40% of international trade was duty-free, while about 10% faced tariff charges of over 10%.[10] In EU-US relations, more than half of the trade is duty-free, while the remaining half faces rates from 1-3% to 30% (for goods like clothes and shoes). The EU tariff on motor vehicles is 10%, the US tariff for train carriages is 14%. In extremely rare cases, though, tariffs exceed the actual value of the product: the USA tariff on raw tobacco is 350% and on peanuts is over 130%.[11] This implies that in developed countries tariffs represent a significant trade barrier merely in a few product categories.

The diminution of applied tariffs was paralleled by a similar process concerning bound tariffs (legally binding duty rate caps established for specific product lines). These were agreed on in a series of **rounds** providing a platform for GATT '47. Article II GATT '47 makes these tariff promises (undertakings) binding under international law. The representatives of MS arrived to these rounds with a request list and an offer list and tried to convince countries representing their export markets to reduce tariffs in exchange for the tariff reductions they were inclined to offer. Because bilateral arrangements and concessions were excluded under the MFN Clause of Article I GATT, MS were not able to discriminate among each other. If one MS reduces the tariff of certain products, that reduction immediately and unconditionally applies to all products coming from any MS. Although the promises to reduce customs duties were, in a legal sense, not based on bilateral or multilateral agreements, mutual economic benefits and advantages were apparent, and the system operated on the basis of the logic of *quid pro quo*. States characteristically decreased the tariff rate of a particular product because other states made similar reductions for products being exported by them. This reciprocity is reflected in Article II GATT, which provides that commitments to decrease (maximize) tariff rates (tariff-bindings) are legally binding and may not be unilaterally revoked without duly compensating the affected parties.

WTO members' tariff bindings were included in the Schedule of Concessions and Commitments annexed to GATT 1994 (incorporating GATT '47, so it was basically the same body of rules). The Uruguay Round, between 1986 and 1994, was extremely successful in extending binding coverage: in developed countries bound rates were virtually extended to all products (99% of product lines), same as in transition economies, which increased their binding coverage from 73% to 98%. This was paralleled by a similar process in developing countries, where binding coverage increased from 21% to 73%.[12] Bound tariffs were also significantly reduced, though they remained high in developing countries.

[9] UNCTAD, Key Statistics and Trends in Trade Policy United Nations, New York and Geneva, 2013. p. 5.

[10] UNCTAD, Key Statistics and Trends in Trade Policy United Nations, New York and Geneva, 2013. p. 7.

[11] Factsheet on Trade in goods and customs duties in TTIP http://trade.ec.europa.eu/doclib/docs/2015/january/tradoc_152998.1%20Trade%20in%20goods%20and%20customs%20tariffs.pdf

[12] WTO (2007) World Trade Report: Six Decades of Multilateral Cooperation, What Have we Learnt? Geneva: WTO. 221.

The world's ten largest economies[13] by GDP (representing 80% of world GDP) are characterized by almost full binding **coverage** (except India) and relatively low bound tariffs. The first three economies, EU, Japan and the USA (representing 52% of world GDP) have a less than 5% simple average bound tariff.

	Binding coverage	**Simple average bound tariff**	**Simple average applied MFN tariff**	**Simple average bound tariff of non-agricultural products (NAMA)**	**Simple average applied MFN tariff of non-agricultural products (NAMA)**
Australia	97,05	9,95	2.52	10.96	2.75
Brazil	100	31,36	13.53	30.75	14.12
Canada	99,7	6,52	4.08	5.17	2.16
China	100	10	9.92	9.13	8.98
EU	100	4,97	5.16	3.94	4.19
India	74,42	48,47	13.39	34.52	10.17
Japan	99,66	4,49	4.03	2.51	2.51
Russia	100	7,58	7.15	7.06	6.51
South-Korea	94,89	16,47	13.90	9.83	6.76
USA	99,94	3,43	3.48	3.22	3.20

Source: WTO, data of 2016[14]

It shall be added that the actual tariff rates are usually considerably lower than the bound tariffs, which at times might produce a huge difference (overhang) in case of countries having a high bound tariff rate. For instance, India has exceptionally high bound tariff rates (48.47%) but a lower simple average applied MFN tariff rate (13.39%) than Brazil (13.53%) and South-Korea (13.9%), which have otherwise considerably lower bound tariffs (31.36% and 16.47% respectively). Interestingly, China and

[13] Based on the 2017 GDP data (current prices, U.S. dollars) of the IMF data, available at http://www.imf.org/external/pubs/ft/weo/2018/01/weodata/index.aspx.

Country	**GDP**
Australia	1,379.548
Brazil	2,054.969
Canada	1,652.412
China	12,014.61
EU	17,308.862
India	2,611.012
Japan	4,872.135
Russia	1,527.469
South-Korea	1,538.03
USA	19,390.6
Total	64,349.647
World	79,865.481

[14] WTO, International Trade and Market Access Data, available at: https://www.wto.org/english/res_e/statis_e/statis_bis_e.htm?solution=WTO&path=/Dashboards/MAPS&file=Tariff.wcdf&bookmarkState={%22impl%22:%22client%22,%22params%22:{%22langParam%22:%22en%22}}

Russia, though developing countries, have a modest average bound tariff (10% and 7.58% respectively), and their actual tariff rates are close to the ceiling (9.92% and 7.15% respectively).

> Traditional measures of trade restriction are customs duties (tariffs) and quantitative restrictions.

The above numbers demonstrate well that in global trade **traditional tools of trade restriction** (such as tariffs and quantitative restrictions) no longer have a significant role. Quantitative restrictions have been banned already by GATT '47, while tariffs have been gradually decreased by MS. Developed countries apply very low bound tariffs, in particular as to non-agricultural products (except Australia where the simple average bound tariff of agricultural products is 3.44%, while that of non-agricultural products is 10.96%). This implies that in developed countries the overall significance of tariffs has diminished very considerably (albeit they are still relevant in agriculture and specific economic sectors), and that the prerogative of developed countries to discretionarily use tariffs as an effective tool to restrict imports has been confined to a limited number of products. Nevertheless, developing countries having a huge tariff overhang may continue to make use of this trade policy opportunity.

It is noteworthy that, due to the **most favored nation (MFN) principle**, prohibiting discrimination among WTO MS, tariffs cannot be targeted at products arriving from a particular MS. Developed countries may not increase their tariff rates on products flowing in from developing countries, only the tariff rates of a given product can be increased in general (as non-WTO MS naturally do not enjoy the benefits of MFN). Let us assume that the US government plans to shield American producers from competition created by German imported cars, in this situation they cannot impose a higher customs duty on European Union imports (even less specifically against German imports), but they shall increase American customs duties on motor vehicles in general, which will detrimentally affect e.g. Japanese manufacturers as well.

A similar framework prevails as to **trade in services**. In the application of the General Agreement on Trades and Services (GATS) two obligations apply to the MS based on a separate, express commitments: market access (Article XVI GATS) and national treatment (Article XVII GATS) These commitments have been made by the MS regarding certain sectors, and their relevant commitments are summarized by the Schedule of Commitments. The Schedules of the respective MS set forth, by economic sector, whether the MS at hand undertook to observe the principles of market access and national treatment as to a given sector, and for which of the four modes of supply. Furthermore, the schedules also contain those restrictions and conditions that the MS set when making the commitment. GATS distinguishes between four modes of supply. The first is cross-border supply, when service is provided from the territory of one MS to the territory of another. The second is consumption abroad, when service is provided in the territory of a MS to the consumer of another. The third is commercial presence, in which case service is provided through the business presence of a MS provider in another MS's territory. The fourth is physical presence or presence of natural persons, in which case service is provided by a MS provider through the presence of natural persons in another MS's territory. Similarly to tariff bindings, GATS commitments cannot be revoked unilaterally, except the affected parties are duly compensated.[15]

[15] Article XXI GATS. This happened for example in the US Gambling case. Wohl 2009, 133-134.

The new generation of free trade agreements (eg. TTIP, TPP, CETA, TiSA) not only erases tariffs and quantitative restrictions (as traditional agreements did), but also **opens up national** (regulatory) **sovereignty to international regulation**. It reforms regulatory autonomy and internationalizes certain national competences, which raises serious questions of (democratic) legitimacy. These new-generation free trade agreements cover the whole spectrum of trade (goods, services, technology, capital, etc.) and do not restrict themselves to demolishing traditional trade restrictions (tariffs and quotas), but ambitiously touch every state action with relevance to trade restriction or the economy (e.g. regulatory differences, public procurement/government contracts, or certain fundamental rights issues) in a comprehensive manner.

The blend of the above various political and social factors resulted in a **new age of regional economic integration law**, which intrudes considerably into national regulatory sovereignty and fundamentally re-shapes its basic notions, also necessitating the rethinking of our notions of economic relations, sovereignty and democratic decision-making. Firstly, new-generation free trade agreements address regulatory restraints that are socially rooted and closely intertwined with national regulatory autonomy, thus, entailing a major shift of sovereign regulatory powers onto international governance. According to a radical opinion, "[*t*]*hese agreements are no ordinary free trade deals*; *they raise questions about the political future of independent nations*, *about sovereignty*, *democracy and indigenous self-determination*, *and*, *above all*, *the people's right to know what governments are doing*."[16] Secondly, while the excessive promotion of free trade may suppress local legitimate regulatory policy considerations and may display free trade as unregulated trade in the eyes of the local electorate, impairing the legitimacy of the notion of free trade,[17] seemingly non-discriminatory regulation is frequently used by local economic interest groups to cut out foreign trade.

12.3.1. Free Trade, National Interest and International Governance

All free trade systems, including the WTO, allow states **to restrict trade** if justified by a legitimate local interest. States may introduce standards, shape taxation, impose public (utility) service duties on enterprises or maintain monopolies in a way that restricts trade and free competition. Since the regulatory frameworks contain vague and fluid concepts and notions, states are normally afforded a wide margin of appreciation and the application of the law becomes a social and mental process, blending economic, social and legal considerations and aspects.

Among others, there is one constant element in the world's free trade systems: they forbid MS from restricting free trade and competition, but allow this in cases where restrictions are justified by a **legitimate local interest**. In these systems, courts face similar issues, as they shall decide in cases that are not only similar, but sometimes exactly the same.

We can observe differences between the systems in relation to what **constitutes a trade restriction**. In this regard, the law of the EU internal market is quite strict: even non-discriminative measures are forbidden, in case they restrict trade. In other words: measure that restrict market access for imported goods (services, investments, etc.) are forbidden, even if they equally restrict the market access of both imported and domestic goods, services, investments, etc. As a result, the measures adopted by a MS could be in violation of free movement, even when there is no protectionist motivation behind them.

[16] Kelsey 2010, back cover
[17] See e.g. Kelsey 2012, 1719.

In contrast, Australian internal market law is based on forbidding protectionist measures, and it mostly considers discriminative measures as protectionist. If the actual purpose of the MS regulation is to determine some sort of product or service standard or some standard related to commercial activity, then it is not usually based on protectionism, and does not infringe the free trade clause under Article 92 of the Australian Constitution.[18] Under the dormant commerce clause of the US constitution, measures that are non-discriminative but disadvantageous to international trade may violate the constitutional ban, in case they restrict interstate commerce disproportionately compared to the local public interest. However, when it comes to non-discriminative measures, states enjoy a wide margin of appreciation,[19] and mainly discriminative measures are quashed by the courts.[20]

If a state measure qualifies as restrictive of trade, it can still be valid, provided it is justified by (legitimate) **local public interest** and it is **proportionate**. Determining whether a measure is proportionate requires a complex examination, because it involves comparing different types of values: free trade on the one hand and some legitimate local interest (public health, morality, environmental protection, etc.) on the other. Comparing these different types of values is essentially a political question, not a legal one, so it is difficult for courts to handle it.

The various systems developed different methods for examining the question, which **encroach upon state discretion with varying intensity**. From this perspective, the CJEU's practice seems quite interventionist: it does not hesitate to balance the value of legitimate local interests (ends) with the principle of free movement. In contrast, the US Supreme Court, which claims to engage in balancing (as it compares two different types of values to each other), practice has shown that in case of non-discriminative measures, if the state can present credible justification for the introduction of the measure, the court will accept it, based on the wide margin of appreciation afforded to states. However, discriminative measures are almost viewed as *per se* unlawful, and although there is a theoretical possibility for justifying these through public interest, there is only a slight change it will pass 'judicial scrutiny'. The most accommodating solution, unsurprisingly, is the one in WTO law, since WTO is a global system based on principles of international public law, in contrast to the domestic US dormant commerce clause or the *sui generis* EU law. In WTO law, the analysis used in cases where the question of local public interest arises is not considered a test of proportionality, but rather an investigation into possible less restrictive alternatives. Here, the relevant question will be whether the state, to achieve the given end, had the option of introducing an alternative measure with the same effectiveness, but less restrictive to trade.

The test of proportionality could be best represented **through an example**. In the US, chlorine was used to disinfect slaughtered chicken. As a result, notwithstanding every effort to the contrary, the chickens meant for human consumption retain a small dose of chlorine, which gets into the human body through the consumption of the meat. The restriction of trade concerning these goods can be justified by both public health, and consumer safety reasons. Based on the intensity of state intervention, three regulatory options can be identified. First, the state can decide not to regulate these goods. In this case, trade in the value of 30 million Euros will be realized, while 1 million consumers will unknowingly buy chlorinated chicken yearly. Second, the state can ban the product entirely. In this case, there will be zero trade but also zero consumers who unknowingly bought a potentially dangerous product. The third option is an intermediary one: the state can demand that consumers be informed about the chlorination through warning signs placed on the product. In this situation, trade valued at 10 million Euros will be realized, but there will also be 100,000 consumers every year, who will not read the warning and will

[18] *Cole v Whitfield* [1988] HCA 18; (1988) 165 CLR 360, 2 May 1988
[19] *Pike v. Bruce Church*, *Inc*., 397 U.S. 137 (1970)
[20] See CTS Corp. v. Dynamics Corp. of America, 481 U.S. 69, 87 (1987)

buy the product with the mistaken belief that it does not contain chlorine (which they would not buy if they were aware of this fact).

If we compare the three different regulatory approaches, we can see that although warning signs are not as restrictive as a complete ban, they do not provide the same level of protection (100,000 consumers) as the latter (zero consumers). However, it does restrict trade to a significantly lesser extent (trade in the value at 10 million Euros will be realized, while the complete ban will result in zero trade).

When comparing these options, the court needs to decide whether trade in the value of 10 million Euros is more important than 100,000 consumers, and their potential health issues. Thus, the court must make a value-based judgment to answer this question. In contrast to the test of proportionality, the WTO-approach investigates whether there was a less restrictive alternative. In this case, the WTO dispute resolution panel will examine whether there was a less trade-restrictive alternative measure (warning signs), which can provide the same (or essentially the same) level of protection as the complete ban, considering that the one has 100% effectiveness, while the other has a 90% ratio of success.

12.3.2. Value Standards

While, at first glance, **fundamental rights** might not appear to be relevant to free trade, (and there is no international endeavor to create a global regime for these universal values),[21] states have realized that compliance with fundamental rights requirements has economic effects because it has cost implications, and domestic producers are put at a competitive disadvantage if they shall comply with higher standards. It is not a surprise that, for instance, labor[22] and environmental standards have become major issues of world trade.[23] Furthermore, rule of law, transparency, and due process (fair trial)[24] became hot issues mainly for similar reasons. International (inter-state) dispute resolution can mainly address national rules and visible government actions. The net of free trade law can scarcely catch under-the-radar violations such as hidden discrimination and undue influence on judicial proceedings.[25]

Of course, **there is nothing new under the sun**. The proliferation of free trade agreements just brought an old phenomenon to light. At the time of establishing the EEC, the founding fathers have set in stone equal treatment for men and women as a principle, which appeared unfit for the founding treaty of economic inspirations due to its rather fundamental-rights character. However, if we observe the circumstances of the adoption more closely, we can see that France insisted on accepting it based on purely economic reasons. The principle of equal pay was well entrenched in French law and France feared that French enterprises would suffer a competitive disadvantage, if other MS allow women to be paid less.

Trade policy protective of fundamental rights may appear not only in the negotiation phase, through linking trade concessions to the protection of fundamental rights, but also in **justifying trade restrictions**. Under WTO law states may be possibly allowed to restrict trade not only based on the products' characteristics but also the process used to produce the goods even if the process itself did

[21] See Aaronson–Zimmerman 2006, 998.

[22] See Alston 2004, 457.

[23] See European Parliament, Resolution of 25 November 2010 on Human Rights and Social and Environmental Standards in International Trade Agreements, (2009) 2009/2219(INI), 15(a).

[24] Wolfe 2003, 157.

[25] Sally 2007, 8.

not affect the characteristics of the product/goods. Although the relevant cases emerged in the context of the protection of the life of animals,[26] this practice may open the door other local values, too.

12.3.3. Investment Protection: Substantive Law and Procedural Mechanisms

The **first investment protection treaty** (Germany-Pakistan Treaty of 1959) was meant to convert certain constitutional requirements (such as expropriation, and protection of legitimate expectations) into international obligations to guarantee them. Consequently, the first bilateral investment protection treaties were normally concluded between developed and developing countries and led by the concerns regarding the latter's legal systems. The obligations assumed were, as a matter of courtesy, mutual, that is, reciprocal. However, these treaties did not aim at establishing higher or in any sense different investment protection standards than the ones already part of the constitutional traditions of Western democracies. The rationale was to convert the relevant constitutional rights and principles into international law guarantees in the form of bilateral agreements, so they could not be nullified unilaterally.

Nonetheless, despite all effort, there was no global agreement and especially no uniformity as to investment protection standards. It is noteworthy that although goods, services and knowledge (intellectual property) are regulated in the WTO framework, investment issues, including investment protection, were almost entirely left out, except the relatively insignificant provisions of TRIMs.

The major turning point was when even developed democracies started concluding bilateral investment treaties with each other. Today, investment protection has become an integral part of new generation free trade agreements, some of which are concluded between developed democracies (Canada, European Union, United States). With this, the guarantee function faded into the background, and investment protection law became **fully detached from its original *raison d'être***.

Albeit investment protection, at least as far as substantive standards are concerned, has always remained bilateral, without a realistic chance of a multilateral system, during this half-century, created a labyrinth of bilateral investment protection arrangements, and **international investment protection took a life of its own,** not acting as the alter ego of national constitutional requirements but as an autonomous parallel system. Furthermore, investor-state arbitration subjected genuine public-law disputes to an arbitral procedural pattern, initially designed for purely commercial disputes, which is devoid of democratic legitimacy due to its secrecy, non-transparency and *ad-hoc* nature.[27] The above developments were topped by new generation free trade agreements, which are blamed for introducing too flexible standards and the attached dispute settlement mechanism lacking democratic legitimacy into relations between developed democracies.

The major sources of uncertainty are the investment protection treaties' '**treatment provisions**' including fair and equitable treatment, security and protection, non-discrimination and national treatment. These principles center around fluid concepts, and confer extremely wide powers on arbitral tribunals to review national policy decisions and national administrative and judicial proceedings. The doctrine of legitimate expectations, deduced from the fair and equitable treatment standard, may raise separation-of-powers issues: a state may be called to account for breaking the promises the executive made also as regards issues falling under legislative competence.

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[26] United States – I*mport Prohibition of Certain Shrimp and Shrimp Products*, WTO Doc WT/DB58/AB/R; Dispute Settlement Panel Report On *United States Restrictions On Imports of Tuna*, 30 I.L.M. 1594, 1599 (1991).

[27] Cf. Weiler 2014, 963.

The above developments were **topped by new generation free trade agreements** which treat investment arbitration as a constant element.

12.3.4. Standards and Regulatory Cooperation

Nowadays, the **most important hurdles to trade** are not traditional trade restrictions but **regulatory disparities** between national technical, sanitary, consumer protection, environmental etc. standards. While there is a general understanding that discriminatory measures should be prohibited, the status of non-discriminatory measures is dubious. The more tolerant approach opens the way to veiled protectionism, while the more interventionist approach goes hand in hand with the risk of subordinating local regulatory values to free trade. New generation free trade agreements champion **regulatory coordination**, which also raises sensitive issues of democratic legitimacy.[28]

Under EU law, even non-discriminatory measures are prohibited, if they restrict trade, while the regulation of the Australian internal market builds on the prohibition of protectionist measures, and here, mainly discriminatory measures are considered protectionist (with discrimination either being legal or factual). In the US, primarily discriminatory measures are caught in the net of judicial control based on the Dormant Commerce Clause, though measures detrimental to interstate commerce may also be prohibited, if they restrict interstate commerce to an unambiguously excessive extent compared to local public interest. WTO law fundamentally prohibits discriminatory state measures and the prohibition of non-discriminatory measures is limited. Accordingly, the tolerant approach opens the way to veiled protectionism and preserves the partitioning of the free trade area along national borders. At the same time, the interventionist approach subordinates local public interest to free trade and may entail legitimacy issues. All these approaches have their merits and drawbacks and they both point to regulatory coordination being the best solution. There are some regulatory disparities that are attributable to serious differences in terms of public policy (such as GMOs or hormone treated beef); however, there are no exigent circumstances behind many of the differences between standards, they are due to diverging traditions and randomness (such as the size of fenders or the color of turn lights).

12.3.5. Regulatory Sovereignty and Protectionism

The purpose of the states' margin of appreciation is to preserve regulatory autonomy and the free trade system's legitimacy, since the excessive promotion of free trade may suppress legitimate local regulatory policy considerations. Although states are granted a certain margin to enforce local values, **this also implies the risk of disguised protectionism**, since regulatory decision-making is frequently impregnated by nationalistic and protectionist trade interests. Although this flexibility is meant to ensure that states have the appropriate margin of appreciation to protect public interest and to enforce local values, it also implies the risk of protecting the market. Under the veil of good faith balancing, regulatory decision-making is frequently impregnated by nationalistic emotions and protectionist lobbying activity; thus, this wide margin of appreciation increases the possibility of these dysfunctions.

While some authors argue that only those measures should be prohibited where protectionist intent is proved,[29] the question remains, how can veiled protectionism be uncovered? One cause of the problem is that the background of accepting state measures often resembles the 'Baptist-bootlegger' coalition. Both support Prohibition – the former for moral, the latter for business reasons (if Prohibition were to be lifted, the bootlegger would lose its market). Thus, e.g., if a country blocks the import of shrimp

[28] As to financial services, see Bickel 2015, 557.
[29] Regan 1986, 1091.

because the technique used for harvesting them affects sea turtles adversely, this may be supported both by animal rights organizations and fishing companies. The latter may be less concerned about the life of sea animals and more about their local market.[30]

> The background of restrictive state measures often resembles the 'Baptist-Bootlegger' coalition. Both support the prohibition – the former for moral, the latter for business reasons (if the prohibition were lifted, the bootlegger would lose its market).

[30] See e.g. United States – *Import Prohibition of Certain Shrimp and Shrimp Products*, WTO Doc WT/DB58/AB/R; Dispute Settlement Panel Report On *United States Restrictions On Imports of Tuna*, 30 I.L.M. 1594, 1599 (1991).

QUESTIONS FOR SELF-CHECK

1. When did the current age of world trade begin?
2. Can states use quantitative restrictions?
3. What do bound tariffs mean and what is their importance in world trade?
4. In what lies the novelty of the new generation free trade agreements?
5. What value standards are contained in the new generation free trade agreements?
6. What is the essence of investment protection law?
7. Why is international cooperation important in the field of standards?
8. What is the relationship between regulatory sovereignty and protectionism?
9. What is the 'Baptist-Bootlegger coalition' in international economic relations?

RECOMMENDED LITERATURE

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