The Rule of Law in International Economic Relations

A government of
laws and not of men
(John Adams)

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Ladies and Gentlemen, dear Colleagues, Dear Alumni and Students:
No lawyer in this room will question the rule of law. It amounts to the most important pillar and foundation of the legal order. It is axiomatic to what we do and live as a legal profession. And yet, a closer look reveals that the concept is not a matter of course. It needs to be regained every day, and at all the time in addressing other social forces, in particular power. Also, the notion is not entirely clear. It goes way beyond the command of the law as a political tool. In domestic law, the terms of *Rechtsstaat* or *état de droit* primarily relate it to the core of the state and its functions. In constitutional settings, the rule of law requires legal authority for state action. It stands for the wider proposition of protecting human dignity, liberty, property rights as bulwark against arbitrary and capricious rulings, but also of protecting minorities from unfettered majorities in democracy. It is an essential building block of federalism, allocating powers to different layers of government under the constitution. It is not limited to positivism, but entails essential principles of government. At the heart of it are the separation of powers, checks and balances, and foremost judicial review of government action and the independence of courts of law.

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In international law, absent statal and strong organizational structures, the notion and aspiration of the rule of law is more modest. In a system which is largely treaty-based and relies upon consent, the rule of law amounts to the principle of *pacta sunt servanda*. No more, but also no less. In international law, it today is essentially reduced to positive law, entailing treaties, but also customary law, general principles of public international law and general principles of law. Under the rule of law, states are obliged to comply with obligations incurred. They are entitled to make good use of rights granted. Rights and obligations are to be respected by governments. They are to be respected by courts of law, both international and national, one would assume. Courts of law and the legal profession are the main guarantors of the rule of law. They are the guardians and play a critical role. An inquiry into the rule of law in international economic law therefore will essentially be an inquiry into the role of courts and lawyers in the game.

Today, international economic law and relations comprise a large part of public international law. Trade, finance and investment law are at the heart of it. But the field today includes all areas related to economic activities and production factors: property, taxation, labour standards, social and economic rights, environmental law and principles of sustainable development. The field cannot be dealt with in isolation, and boundaries to the broader areas of public international law remain vague and fluent. An inquiry into the rule of law cannot stop short of other key areas of public international law, such as the law of the sea. Today, I shall essentially focus on trade and investment law.

A. From Foreign Policy to International Law

Trade and market access has been at the forefront of building international agreements. Many treaties and compounds, ever since the Greek period, have dealt with the subject. The 1798 US French Treaty of Amity and Commerce consolidated the principle of most favoured nation treatment. It informed much of the 19th Century trade agreements, beginning with the French-UK Cobden-Chevalier Agreement in 1860. The principle of national treatment informed a subsequent generation of bilateral Friendship and Navigation Treaties. Intellectual property was the first area to be addressed by multilateral agreements with the Paris and the Berne Conventions of 1883 and 1886. And yet, all these areas did not make it to the heart of public international law. Trade and investment played a minor role in public international law doctrine, compared to the law of the sea addressing navigation and natural resources. Leading textbooks on international law would not deal with trade law extensively. Intellectual property, for example, was rather considered the field of a separate epistemic community mainly interested in domestic commercial law and contracts.

After World War II, international trade, perhaps due to the failure of the Havana Charter establishing an international Trade Organization, did not attract the interest of public international law in a comparable manner to the law of the UN, or the Bretton Woods institutions. The 1947 General Agreement on Tariffs and Trade was

hardly noticed in academia, until John J. Jackson expounded its genesis and legal complexity in his seminal work *World Trade and the Law of GATT* published in 1969. It took two generations of lawyers, many of them trained at the University of Michigan Law School, to introduce the field and, eventually, to conquer a central place in contemporary public international law. The effort was supported by extensive writings and leading journals, in particular the *Journal of International Economic Law* founded in 1997, and new training programmes, such as the Master of Laws in Saarbrucken, Barcelona or Washington DC, or at the World Trade Institute in Bern. Much of the boost was due to the end of the Cold War, the completion of the Uruguay Round of multilateral trade negotiations and the foundation of the World Trade Organization in 1995.

Other than trade, investment law and property protection has been the topic of arbitration throughout the 19th and 20th Century. The field reached particular prominence and a central position in public international law with the advent of bilateral investment agreements as of 1959. These agreements introduced standing for private companies. In parallel to the agenda of protecting human rights, public international law began to reach beyond the state and actively include and entitle private persons by means of derived and granted property rights. This was an important extension of the rule of law beyond intergovernmental relations. Today, the field is at the heart of public international law.

For a long time, international trade relations were considered to be part of foreign policy and thus the prerogative of the executive branch, with the noble exception of the US constitution which empowered Congress to set the main rules. The field was dominated by diplomacy and the growing economics profession in trade negotiations, engaging in a long-term process of reducing and eliminating tariffs as a particular form of taxation of imports and exports alike. Principles and concessions were enshrined in international agreements. They were managed in trade policy by diplomacy, in negotiations and largely dominated by power politics, led by the United States after World War II. Lawyers, as a profession, were largely absent at the time. And so was the rule of law. After the fatal Advisory Opinion Nr 20 of 2nd September 1931 by the Permanent Court of International Justice, prohibiting a customs union between Germany and Austria under the Versailles Treaty, international courts were largely absent in shaping trade law in the post war era. And so was legal doctrine. In practice, this started to change with the creation of legal services in the GATT secretariat in the 1980s, increasingly supporting negotiations, dispute resolution panels and shaping legal procedures. With the advent of the World Trade Organization and the Dispute Settlement Understanding, the legal approach was corroborated. Panels reports increasingly were based upon legal argumentation, rather than offering diplomatic settlement. The establishment of the Appellate Body as a compromise by the United States and the European Union to accept binding arbitration introduced a proper and highly innovative two-tier legal system. Parties henceforth were entitled to be represented by private counsel. The participation of large law firms specialised in trade further refined the legal approach to dispute settlement and its quality. The rule of law, finally, had arrived in the field, linking trade

and non-trade concerns in a vast and impressive body of case law. The case law, in turn, drew the attention of legal scholars and public international lawyers and paved the way to achieve a central status in contemporary public international law of importance beyond trade-related issues. It is noteworthy that compliance with WTO rulings was high, except for a number of highly politicised cases, such as *EC – Hormones* or *US – Tax Treatment for "Foreign Sales Corporation"*, all which required legislative changes by Parliaments and could not be settled by the executive branch by adjusting regulations or practices. As much as damages are available for failure to comply in domestic law, WTO offers the options to withdraw concessions and to rebalance the system by means of countermeasures, but only upon authorization of the membership and not unilaterally.

Likewise, the rule of law developed in the field of investment protection. An increasing number of bilateral private-state arbitrations under today 2270 bilateral investment agreements (BITs) in force under the umbrella the ICSID Convention, UNCITRAL and ICC produced panoply of decentralised case law, applying these bilateral agreements with all its variants. Fair and equitable treatment and property protection gave raise to challenge governmental policies, often addressing environmental or health concerns.

The rule of law and lawyers became to dominate the two fields in litigation.

B. The Advent of Case Law

The political debate on the legitimacy of the WTO following the 1999 Seattle Ministerial meeting focused on North-South relations and environmental concerns. It challenged a narrow reading of trade and investment rules. It brought about a wider reading of exceptions and stronger considerations of non-trade concerns in the emerging case law, founded by the seminal case of *United States — Import Prohibition of Certain Shrimp and Shrimp Products US-Shrimps Turtle* in 1998. The case law demonstrated that WTO agreements are well calibrated and include the necessary safeguards to protect non-economic concerns. In due course, exceptions were no longer narrowly construed but placed on par with the principles of non-discrimination. Linkages to other agreements were made, and can be further strengthened in applying and interpreting WTO agreements.

Likewise, *ad hoc* arbitration in investment expanded regulatory space of governments to address labour and environmental concerns. But questions of consistency called for the introduction of an appropriate appeal mechanism in comprehensive economic cooperation agreements, such as CETA, with a view to bring about greater coherence. The WTO Appellate Body clearly served as an example to this effect. While this issue has not been resolved, it is fair to say that a new and proper balance of rights and obligations emerged in case law and more recent agreements which place trade and investment in the broader agenda of sustainable development. It is likely to do so also in the context of climate change mitigation and adaption under the emerging principle of common concern of humankind. Trade and investment law, in other words, developed from strictly purposive systems focussing on

trade liberalization and protection of foreign direct investment to what may be called modest constitutional frameworks. They are able to balance competing interests and support the process of sustainable development and management of human, financial and natural resources.

I do not think that these developments can be separated from the fascinating evolution of legal protection in the European Economic Communities, today the EU, and the central role of the European Court of Justice in Luxembourg, as well as the Strasbourg European Court of Human Rights under the Council of Europe. Both institutions, created in response to the failure of the rule of law in European fascism, set an example and strongly contributed to the effort to bring about the rule of law also in the field of trade and investment. While lessons cannot be readily drawn from EC law for the international realm due to different aspirations and levels of integration, the European experience in particular shaped the attitudes of European lawyers in the field and their dedication to strengthen the rule of law in the international realm.

Today, the main challenge of the rule of law in WTO law occurs in the field of trade remedies. It comprises anti-dumping, subsidies and safeguards. The United States takes issue with narrow interpretations and refuses to renew the Appellate Body (AB) of the WTO. It is a bipartisan view in the states that the AB had overreached its powers. As a consequence, the dispute settlement system of the WTO is essentially back to GATT days when a party was able to reject the adoption of a report, today by appealing the findings of a panel into the void. The rule of law took a serious blow. A number of Parties, including the EU, China, Australia, Canada and Switzerland created the Multi-party Interim Arrangement (MPIA) which today is ready to receive appeals on the basis of the arbitration clause of the DSU. 25 Members (a total of 52 states and almost a third of WTO Membership) joined the arrangement. First cases are expected in 2022. At the same time, WTO members seek to reform the dispute settlement system and recalibrate the role of panels and the Appellate Body in redefining appropriate standards of review. No progress has been made so far in recalibrating the dispute settlement system.

C. The Legacy of Distrust

The attack on the Appellate Body and binding dispute settlement expresses deep concerns over the legitimacy of the system, the rule of law and thus the role of lawyers. While focussing on trade remedies and national security, reasons go deeper. They relate to sentiments of unfairness, the experience of neoliberalism and the financial crisis, the stalemate of negotiations, and the rise of China and of populism in the West. The latter revives nationalism and rejects the rule of law in international economic relations.

First, many in civil society continue to question freer trade and the legitimacy of WTO law, ignoring the calibration of the agreements and the protection of non-economic concerns in case law. The results of the Uruguay Round were mainly shaped, in the aftermath of the breakdown of the Soviet Union under neoliberal

theory and the Washington consensus stressing liberalization, privatization and deregulation. They are considered detrimental to the poor and the environment in an age of increasing income and wealth disparity. The subsequent Doha Development Agenda failed to produce correcting results and left developing countries largely frustrated, despite increasing trade shares. The financial crisis of 2007 to 2012 demonstrated the pitfalls and shortcomings of neoliberalism also within industrialised countries. Insufficient consideration was given to deindustrialization and the fate of poorer and often rural strata of society. Trade policy limited to liberalization no longer was sustainable and undermined the rule of law. It gradually turned to trade regulation while public perception of trade policy failed to recognise the shift to constitutionalisation. We still speak about free trade agreements rather than economic cooperation agreements.

Second, the lack of progress in addressing new issues, such as the digital economy, climate change and energy risks show that the rules of WTO law no longer are responsive to contemporary and future needs and are increasingly outdated. New disciplines are called for. While the principles of non-discrimination and transparency remain crucial, more detailed rules need adaption. Their application under the rule of law risks producing adverse results, undermining the legitimacy of international economic law.

Third, the accession of China to the WTO in 2001 fundamentally undermined traditional transatlantic leadership in international economic law. It moved the system to a multipolar world, and more recently to a bilateral world with the United States geopolitically competing with China, leaving the World, including Europe, in between. China, while stressing the importance of multilateral disciplines in the WTO, openly defies the rule of law in the law of the sea, claiming the South China Sea as territorial waters. Tensions increased, and mutual trust vanished.

Fourth, the rise of populism in response to neglecting domestic inequalities produced by globalization, neoliberalism and the advent of global value chains. It strongly harmed the rule of law. Populism seeks a return to government by strong men and authoritarianism, ignoring the importance of institutions and defying the rule of law. These attitudes clearly dominated Brexit which was a major blow to multi-layered governance, market integration and European political stability. Such attitudes informed the Swiss Government to reject a much needed framework agreement with the EU, including binding legal dispute settlement. They dominated US Trade policy under the Trump Administration and inspired authoritarian governments around the world to follow suit. The trade war of the Trump Administration was a climax of unilateralism, defiance of multilateral rules and dispute settlement. The paradigm, so far, has not fundamentally changed under the Biden Administration, despite repeated assurances of cooperation and multilateralism. There remains a suspicion against the rule of law operating under a system which does not sufficiently take into account contemporary needs of domestic politics and policy. There is a suspicion that the rule of law amounts to the rule of lawyers.

Recent evolutions remind us that the rule of law is subject to cycles in interacting with power and powers. The lack of firm and central institutions in international

economic law render it vulnerable und open to challenge. The primacy of national interests and an increasing invocation of national security risk undermining the entire multilateral legal system. The conviction that the 1930s of the 20th Century are firmly behind us, no longer stands.

Sceptics of international law are reassured. They again may claim that international law is at the hands of power politics and should not be considered law in the Austinian tradition of legal philosophy. They argue that it is succinctly different from true, enforceable domestic law, and thus from the rule of law.

D. The Legitimacy of International Economic Law

All these objections essentially question the legitimacy of international economic law, upon which the rule of law depends. It can only be claimed if laws are basically fair and just. Otherwise, they are ignored or circumvented.

I submit that today's principles and rules of international economic law, despite many open issues and problems, essentially live up to basic fairness and justice. Non-discrimination is an emanation of the fundamental principle of equality. Open trade and foreign investment are emanations of liberty and instruments to maintain peaceful relations among nations who settle their differences by law and if need be, by recourse to legal litigation under the rule of law.

I recall that this body of law allowed for the substantial increase of overall trade shares of developing countries and emerging economies, lifting millions out of poverty. It is almost 50/50 today. It strengthens purchasing power of consumers, in particular of lower income strata. It offers the foundations of bilateral and plurilateral agreements building upon the common law of international law. It allows building bridges between different political regimes and maintains a minimal level of trust, reducing the risk of warfare. Since the financial crisis of 2007 to 2012 and the ascent of sustainable development, a better balance between economic, social and environmental concerns emerged. Trade policy no longer is limited to liberalization but essentially deals with trade regulation, balancing different interests at stake.

Voluntary compliance is high. States continue to voluntarily honour international commitments most of the time (*Louis Henkin*) out of self-interest. Otherwise, complex societies and interaction in terms of communication and commerce, would not work any longer. The overall status of international economic law cannot be measured by just looking at tensions and piques of non-compliance, and leave the broader and flatter landscape of day to day operations aside. Millions of transactions continue to be daily based upon the multilateral trading system, as a matter of course. Brexit has shown the practical implications when such rules no longer work, much to the detriment of small businesses and consumers alike.

The body of existing law offers the basis to further developing the rules in order to address contemporary and future needs of sustainable development and common concerns of humankind, in particular, natural resources, renewable energy, climate change mitigation and adaptation, They all strongly depend upon transfer of tech-

nology and the modalities of the international trading, financial and investment system.

The existing body of law allows building closer linkages between trade, investment and competition. Many issues of distributive justice, often homemade, remain to be addressed: the fate of least-developed countries, short of tradable goods except commodities, access to medicines and vaccines, to the problem of increasing income and wealth distribution within states as a matter of international law. The point is that all this can be built upon the foundations of existing law. We should trust this foundation, and in doing so recognise the rule of law.

Some of these issues can be addressed within existing agreements. They set out principles and rules, but also take into account non-economic concerns which states protect in negotiations and defend in litigation. Construed in the spirit of *US – Shrimps Turtle*, they offer an appropriate balance of interest. The methodology developed by panels and the Appellate Body, and courts of arbitration, supported by scholarly work, offers a framework of comprehensive analysis of all factors involved, including the need for safety values and safety nets. If states make no use of them, this is in their own responsibility. If they do, international law will be concerned with calibration with a view to avoid unnecessary restrictions and rent-seeking protectionism detrimental to general welfare.

E. Scope and Standards of Judicial Review

The way international economic law is developed and applied, taking into account non-economic concerns, amounts to what may be called modest constitutionalization. What imports is not the term, but the intellectual mind-set of shaping and applying the principles and rules with the broader context in mind. WTO law allows doing so, indeed requires doing so. It cannot flourish under a functional approach of different international organizations each operating on its own and in isolation. Moreover, the rule of law cannot be limited to expounding and applying specific rules in isolation. It needs taking into account other and related agreements and general principles of law, such as non-retroactivity, proportionality, good faith and the protection of legitimate expectations and equity as a means to correct unfair results produced. It requires taking into account human rights and principles of sustainable development. All this is possible under the rules of the Vienna Convention on the Law of Treaties.

While broadening the scope of review, we need to carefully calibrate standards of review at the same time. Often, but not always, different interpretation of principles and of rules are possible. Unlike the laws of nature, the law is not entirely predefined. It is the product of human processes and experience. It frequently needs further specification in the legal process, under the facts of a case. In applying principles and rules, these are further developed in case law one way or another within the bounds of the principles or rules concerned and applied. Rarely, there is just a single answer. Different views exist in pluralist society.

Standards of review therefore are essential in defining the role of lawyers and in avoiding that the rule of law transgresses into the rule of lawyers.

The legitimacy of the rule of law and of lawyers in this process primarily consists of deterring and preventing the abuse or rights and obligations by governments or domestic courts in international relations. As long as these operate within reasonable bounds and margins of appreciation, the fundamental requirements of the rule of law are met. Judicial review of government policies, in particular in trade remedies, should therefore essentially operate under a standard of review limited to reasonableness. This process includes the exposition of a proper benchmark in deciding whether or not there is a violation of international law. The benchmark possibly guides subsequent interpretation and application *obiter dictum*, but does not necessarily overrule the governmental decision at hand if and to the extent it meets standards of reasonableness. Full and *de novo* review should be limited to what I call constitutional issues, including the interpretation of general principles, the relationship of different agreements and where a uniform interpretation is essential for the overall operation of the legal system.

A doctrine of self-restraint will also help anchoring more firmly international economic law in domestic law. Here too, it plays an important role in checks and balances and avoiding arbitrary and capricious decisions by authorities.

F. The Role of Domestic Courts of Law

In international trade and investment, the rule of law mainly relies upon domestic, transactional law of commerce, contracts and torts. It is here that judges and lawyers are at ease to implement the rule of law. There is much less litigation on public law trade or investment regulation before domestic courts. Unless transformed into domestic law, domestic courts are often barred from taking international treaties into account. Or, they may refrain from giving direct effect to these rules in defiance to the prerogatives of the executive branch and parliaments. Accordingly, practising lawyers are much less interested to follow international economic law and focus on the transactional side of the field where the rule of law is firmly anchored in domestic law. All this substantially weakens the rule of law in international economic relations.

Domestic courts of law and lawyers therefore should be enabled and empowered to apply international economic law. We need to transgress the fragile fate of the rule of law in international relations by more firmly anchoring it in domestic law. Only once this is achieved, it will no longer be exposed to the vagaries of power politics and a fragile superstructure of international courts of law, organizations and institutions. As any other field of law, trade and investment regulation depend on strong institutions, and these are mainly to be found in domestic constitutional, federal and transnational settings of democracies. Domestic courts are the main guarantors of federalist principles in a system of multi-layered governance. They need to lead the way in following what I call the modest constitutional approach in applying these principles and rules.

International economic law plays an important role in checks and balances and avoiding arbitrary and capricious decisions by authorities. It is a matter of taking international law seriously in daily life. Given its legitimacy and usefulness in international relations, it is difficult to see why international law – being the law – does not automatically apply in domestic law and before domestic courts as a matter of *pacta sunt servanda*. It is difficult to support the doctrine of dualism without weakening the rule of international law as legislators may not fully implement rights granted and obligations incurred. It is difficult to see why international law cannot be given direct effect to justiciable rights and obligations as a matter of principle, as any other rule of law under similar standards of review and self-restraint expounded above. Courts should go beyond the doctrine of consistent interpretation, respecting international law merely the bounds of a given domestic legal framework. At the same time, they should exercise judicial restraint under the rule of reason for similar reasons explained above. They should respect margins of appreciation of government and lower courts in applying international law.

As a corollary, treaty-making has to be democratically inclusive and legislators should be enabled to define relevant principles and guidance for the negotiations by what I call front-loading trade policy. Since domestic and foreign affairs in international economic relations no longer can be separated and are highly interdependent, and more and more issues need to be addressed in international relations, parliaments need to play a role which is able to compensate for the loss of classical legislative functions. They should define the principles in domestic law which the executive branch should seek to implement in international negotiations and agreements. All of this essentially depends upon strengthening international economic law in general legal education.

G. The Importance of Legal Education

The vulnerability of the rule of law is not unique to international law. An increasing number of authoritarian states defy it in the pursuit of power and dominance. Populist movements undermine it, even in democracies. In the end of the day, all law depends on trust and the rule of law is a conviction which needs to be nurtured early on in education, not only of lawyers but of all citizens alike. This is the essence of Plato's *Republic* and of *The Laws* in building an ideal polis. Today, it is anchored in the respect of the individual and human dignity, in the respect of legal institutions and the legitimacy of the law in general. It is anchored in democracy which depends on the rule of law and cannot breathe and live without it, despite the fact that the rule of law sometimes overrules majorities to the benefit of individuals and minorities.

In education, and in particular legal education, we need to convey that the same convictions also apply to international economic relations. They cannot be deployed in a peaceful manner, respecting individuals and countries alike, without the rule of law. There is no fundamental difference between different layers of governance; they all respond to human needs and their interaction depends on the law.

There is no fundamental difference between international and domestic law. That in turn implies that students need to be exposed to international economic law, to its philosophy and details alike. Politicians need to be acquainted with its principles. Practicing lawyers need to develop the skills to work with it in daily life, in particular litigating before domestic courts of law. In a world of specialisation, and given the complexity of the law, this is difficult to achieve. But in the end of the day it is a matter of creating appropriate networks and generate an understanding that there might be a problem of international economic law which could and should be addressed by a specialist in the respective field of law. It essentially is a matter of awareness, basic knowledge networks and organisation. The future is built in educational institutions like yours.

H. Conclusions

In conclusion, when we set out that the rule of law in international economic relations is more modest than under the constitution, we need to revise the statement. We need to be more ambitious and go beyond positivism and the principle of *pacta sunt servanda*.

The legitimacy of international economic law essentially relies upon fostering human welfare by means of international commerce and investment, while preventing rent-seeking protectionism strengthening the protection of legitimate expectations and from abuses of the law detrimental to human welfare. The rule of law depends upon the legitimacy of these principles and rules. These in turn need to be able to take into account all pertinent interests and concerns. In order to be sustainable, a quasi-constitutional mind-set is indispensable which reads principles and rules in context. It requires a legal methodology in international and domestic courts alike which is aware of the role of checks and balances, the interaction of different layers of law and governance, and policy spaces required. These functions in turn depend upon judicial review and enforcement. They can be largely assumed by standards of review within the bounds of reasonableness, respecting margins of appreciation of governments and avoiding the rule of lawyers. *De novo* review will be required to settle issues of constitutional dimensions, requiring uniformity of the law.

This is the way I should like to suggest regaining and building trust in the rule of law and in lawyers in the field. All of this cannot flourish and be secured without a better understanding of international economic law in the general public, and the legal profession in particular. It is a complex area, and much will depend upon you, on your studies and subsequent professional careers. The threat of populism will be a constant companion, and it is up to us to stand up against it, stressing the importance of honest debate and reason. The rule of law will be in your hands.

Thank you for your attention.

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