Crisis, Compromise and Institutional Leadership in Global Trade: Unfair Trade, Sustainable Trade, and Durability of the Liberal Trading Order

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Abstract The transformations of the current liberal order is fiercely order debate among liberals and realists in International Relations (IR). The article examines how the liberal claim of institutional leadership, even in complex networked orders, is challenged by realists and the reality of forum-shifting and institutionalized hegemonic power. Yet, the article advances the constructivists argument that order and leadership rests on the compromise of social purpose and power, even if much IR tends to prioritize the domestic sources of leadership at the expense of international sources of institutional leadership. The substantive issues discussed in the article concerns the current trading disorder of fragmented, unsettled and uncertain trade relationship. The article discussed the future of the trading order in the context of new articulated demands for tougher regulation of environmental and social sustainable trade, and in light of recent modernization debate in Europe on the desirability of US-style enforcement provisions in future EU trade agreements.

Keywords International trade · WTO · Dispute settlement · EU trade policy · Sustainable trade

1 Cracks in the Trading Order

It [the WTO] doesn't matter. Then we're going to renegotiate or we're going to pull out. These trade deals are a disaster, the World Trade Organisation is a disaster.

Donald Trump, quoted in Financial Times (23/7-16), Dyer, 2016.

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If people are not willing to renegotiate in good faith and promote fair trade ... then [Trump] will have some tough decisions to make and I think he's up to the challenge of whatever he believes is necessary to make sure we get fair negotiations and fair treatment in these world bodies, including walking away.
DiMicco, 2017.

Leadership in international trade is in crisis. Leadership has been possible during past crisis but such leadership have always relied on robust, vibrant and effective institutions. Leadership in an era of contested or distrusted institutions is difficult. This article revisits the question of leadership sources in times of crisis. The trade crisis is acute. Existing trade-related institutions, the regime complex of global trade, have been orbiting around the World Trade Organization (WTO) for more than 30 years. The centrality of the WTO is challenged by the shock result from the US election, the contestation of the Transatlantic Trade and Investment Partnership (TTIP) and the annulment of the Trans-Pacific Partnership (TPP). In contrast, the Regional Comprehensive Trade Partnership (RCEP) initiative is not seen as evidence of the declining order (Acharya 2017). Although cracks in the liberal trading order have been exposed, the depth of these cracks is difficult to gauge at this moment. As world trade appears heading into an era of disruptions, uncertainty and fragmentation, the salience the liberal trading order is inevitably questioned. The social purpose and institutional form of multilateralism, especially its dispute settlement mechanism, is at the center of the controversy. The cracks in the order could grow into a paradigm shift of the order. The substantive issue explored in here relates to trade-related sustainability requirements, understood as social and environment-related requirements to exports, production and investments. It asks whether soft, multilaterally embedded and promotional approaches to sustainable trade is being replaced by a hard, conditional and unilaterally based approaches by the trading powers, possibly involving the use of sanctions.

Sustainable trade is a crucial terrain in which the clashes between the post-hegemonic, pre-Trump, liberal trading order and the turbulent, post-Trump trading disorder is played out in. It is testing the WTO to the limit (Hufbauer and Cimino-Isaacs 2015). This policy discussion is inevitably linked to the politics of designing institutions. Should trade sanctions be used to effectively promote certain global policy goals, or to safeguard an economy against unfair competition? An increasing number of Americans and Europeans think so. The rather technical issue of designing appropriate, effective dispute settlement mechanisms in trade agreements has resurfaced dramatically. Liberal institutionalists see the controversy as an issue of facilitative leadership involving complex negotiations on different institutional blueprints. Yet, the paper suggests, the controversy on sustainable trade is best understood as a potential order transformation, a collapse of the transatlantic bargain upon which the WTO was built, reflecting a deep-rooted clash between competing designs, scripts and frames on how to govern trade, and how to determine what 'fair trade' is. It is a clash between softer facilitative leadership, understood as communicative and promotional modes of trade leadership against the harder, uncompromising mode of trade leadership, involving enforcement by possible use of sanctions. In the

absence of an international compromise on sustainable trade, evident in the paralysis of the WTO as well as the International Labor Organization (ILO), the unilateral approach to ensure ‘fair trade’ is gaining much domestic policy attention in the ‘declining’ trade powers, especially in the US but possibly also within EU.

This article starts by revisiting the current liberal order debate among liberals and realists in International Relations (IR), before it examines how the liberals stresses institutional leadership, even in complex networked orders, is challenged by realists expectation of forum-shifting and institutionalized power. Yet, the article advances the constructivists argument that order and leadership rests on the compromise of social purpose and power, even if the domestic sources of leadership tends to ignore the international sources, namely institutional leadership. Preexisting scripts and domestic policy frames are important. These issues are subsequently discussed in the context of new demands for tougher regulation of sustainable trade, on environmental and social sustainability, and in light of recent modernization debate in Europe on the desirability of US-style enforcement provisions in future EU trade agreements.

2 IR Theories on Trading Orders

Current trade relations is in turmoil. There is a leadership void. This could spell a disruption of the liberal trading order, even if an ‘unfair trade war’ remains a remote possibility. It is undesired by business linked up in global production and trade. It is, however, increasingly demanded by the domestic constituencies of the ‘declining’ trade powers. The pace and scope of the reorientation amongst US policy makers towards economic nationalist policy positions has shocked the existing trade policy community. Until now, liberals have pointed to international trade as the foundational stabilizer of an otherwise troubled American order (Ikenberry 2015; Guillén 2016). Facilitative leadership has been possible precisely because it is institutionalized. The world is not only multiplex but also interdependent (Acharya 2014). Disorder is not so much a reflection of the decline of the US, but about the rise of other powers (Zakaria 2009). It will be an order without a center of gravity (Kupchan 2012). The liberal order is not an imposing hegemonic order (Sørensen 2011) but rather one of liberal restraint, and driven by reason, even without leadership. It is, however, characterized by frequent legitimacy struggles. It has not reverted into an imposing, sovereign-insensitive, hegemonic order but evolved into a more loosely fragmented but still rule-based liberal order (Ikenberry 2012). Even such moderate liberal optimism challenged by IR realists (Walt 2016). Kagan (2017) foresees the twilight of the liberal order, echoing the concerns of IR realism on multipolarity. This debate illustrates the deep-rooted preoccupation with the IR discipline with the problem of the declining hegemonic power of the US. However, the liberal trading order has proven itself remarkably resilient in the past.

3 Facilitative Institutional Leadership or Institutionalized State Power?

Trade can cause problems. Cooperation can be difficult. Trade regulation is about balancing sovereignty concerns with common policy commitments. As such, this article shares an understanding of ‘an international order’ with the English School in IR (Buzan 2016; Dunne and Flockhart 2013) as well as constructivist-minded liberals (Ruggie 1982, 1995; Abdelal and Ruggie 2009). Beneath the disorder is a robust set of invisible (or ‘primary’) institutions, which transcends disorder of the observable (‘secondary’) institutions. The trading order has always been fragmented and yet remained surprisingly stable. The non-discriminatory WTO norms, expressed by GATT article I and III (the so-called ‘national treatment’ and ‘most-favored-nation’, respectively), seen in context to other norms, such as rule of law, formal sovereignty and reciprocity. Legal procedures must be followed. Formal sovereignty must be respected. Yet, cooperation is also premised on a negotiated balance of rights and obligations, as reflected in the texts of the WTO agreements. A shared sense of reciprocity among states is a precondition of facilitative leadership.

In contrast, leadership is to realists all about by power projections, securing control over outcomes. State power over institutions is a function of the size, position, domestic preferences, negotiations skills and resources of the particular state. Power through institutions is slightly different. Many liberals largely accept that the decisive source of leadership is domestic politics of the dominant powers. The structure of the system may be a constraining factor. To realists, institutions matter if they advance the leadership. States seek possession of *institutionalized hegemonic power*. Control over an institution solidifies their future power position.

Liberals see *institutionalized facilitative leadership* as an important moderator on such brute exercise of power. It is facilitative power since no coercive power is transferred to international institutions. It encompasses entrepreneurial and intellectual leadership (Young 1991), referring to individual skills, agenda-setting power and learning dynamics within and centered on a particular site. The source of leadership is defined through the interaction between the international and the domestic, structured by institutionalized processes of governance. States not only invest in institutions to gain control over future outcomes but also wants to ensure that others live up to the bargain. States rely on effective solutions to common problems. Institutionalized power leadership in a multilateral order is rare. Multilateralism is an institutional form of facilitative leadership, demanded by most states, precisely because of its inability to be controlled by the larger ones. Facilitative leadership is not only about state leadership (on facilitative leadership, see Zhimin et al. 2017). It is also about assurances for sustained facilitation of cooperative leadership. The institutional form of facilitative leadership matters. It assures functionality, legitimacy and durability. The long-term realization of common goals requires robust, effective and legitimate institutions, beyond the state.

To ensure facilitation of an acceptable consensus on difficult cooperative problems, as evident in the unfair trade debate, firm and durable institutions are needed. Institutions are equipped with specified disciplines, permanent

communication channels and operational conflict resolution mechanisms. Not all institutions work. Some do, however. This has precisely been the case on trade. The trading order has evolved from an intergovernmental GATT regime centered on the American postwar order, reformed into the WTO in 1993, custom unions and bilateral agreements towards a more complex system containing plurilateral agreements, inter-institutional regulatory arrangements, private market arrangements and possibly mega-regional trade arrangements. The density and diversity of institutions, their substantive coverage and geographical scope have transformed what was a simple system of treaty-based regime, easily controlled, into a more complex network of forums, some of which contain hard governance by enforceable treaties, primarily the WTO, and complemented with softer forms of governance, including marked-based corporate social responsibility (CSR) initiatives.

Institutionalized leadership under such circumstances is difficult. State control is impossible. An institutional complex represents an informative step away from thinking in terms of a hierarchical-based power order. Despite the current crisis on trade, liberal institutionalists remain convinced that a fragmenting complex is a more accurate description of the present order. Fragmentation, complexity and diversity do not necessarily produce decline and conflict. Each brings something of its origins and identity into the complex. Each component is formed by and accountable to different constituencies. Each domain coexists. Complexes are fragmented in their very nature, and incoherencies in governance practices can persist. Complexes link national, international and transitional domains together. The emphasis is on positive (or negative) learning rather than conflictual decision-making. Complexes are persistent because of their looser organization and lower transaction costs. However, the research agenda downplays conflicts, be it political or legal. It is an extension of regime concept, rebranded as the ‘regime complex’ approach or ‘contested multilateralism’ (Orsini et al., 2013; Keohane and Morse 2015; Morse and Keohane 2014; Meunier and Morin 2015). Yet, liberal institutionalists fail to specify precisely how conflicts between legal subsystems are mitigated within this network of institutional subsystems. How stable will the conflict be if frequent clashes and shifts between differently equipped legal systems are frequent?

Realists have criticized the concept for downplaying power politics while overstating the persistence of institutions (Drezner 2013) free trade agreements (FTAs), WTO and other trade-related institutions constitute a whole, a complex within which different trade-related institutions communicate with each other, sometimes cooperatively, sometimes competitively. It is silent on direct confrontations. Liberals tend to assume that institutions produce cooperation. The establishment of the WTO in 1993 epitomized this belief. Although the stalled Doha Round (2001–) questioned the relevance of liberal optimism, it never contradicted it. Systemic protectionism failed to materialize after the financial crisis. The liberal optimism is challenged today. Echoing Mearsheimer (1994: 5), the WTO has proven itself to be ‘... a reflection of the distribution of power in the world’ and ultimately ‘...based on the self-interested calculations of the great powers.’ ‘Institutional realists’ have reemerged on the scene; the proliferation of formal institutions produces less cooperation. Drezner (2009: 66) pointed out that regime

complexity dilutes regime ‘focal points’, i.e., the norm, rule or procedure around which actors’ expectations converge (recalling Krasner 1982). Overlapping legal mandates undermined the sense of legal obligation necessary for an institutional order. Initiatives such as TPP, TTIP and RCTP demonstrated that the WTO no longer is ‘a focal point’ in global trade. The trading powers are reorienting themselves. The construction of competing focal points is part of a rational leadership strategy, constructed by trading powers demonstrating leadership. Control of an institution is a power resource. Forum shifts are to be expected in an asymmetrical trade order. Institutions, including dispute settlement systems, only work as long as the powerful want them to work. If not, they are abandoned.

As the WTO no longer serves the interest of the powerful, ‘better’ trade institutions are being constructed. In other words, institutional leadership is transformed into institutionalized leadership. The source of this leadership transformation is located in the domestic politics of trade power. The trouble is that the number of trade powers are multiplying. The liberal trading order is replaced by a multipolar trading disorder. Trump’s threat of exiting the WTO is, therefore, not irrational, to the realist institutionalists. It is, from this perspective, a rational leadership strategy in response to perceived loss of institutionalized leadership. Trump appears to conclude that the WTO no longer reflects the concerns of the US.

If major trade powers are convinced that bilateral liberalization offers a more attractive, cost-effective route to trade liberalization, institutionalized leadership in specific sites in global trade is a better way of controlling future outcomes. To institutional realists, it is essential to understand how the new trade agreements can be designed as more effective market access for their constituencies, equipped to settle regulatory conflicts in favor of the regulatory competitiveness of businesses in the powerful economies. Global trade will not be deregulated as such. It will continue to be regulated, or rather re-regulated. The interesting question is on whose premises. The paradox is that the demands of global businesses are being ignored. Exporters have no interests in fragmented regulation of global trade. It is costly, disruptive and unpredictable. Much of the current turbulence in trade is caused by this clash between the national and the transnational economy, perhaps most visible in the US, but the underlying tension between the territorialized and de-territorialized economy can be observed everywhere.

3.1 Re-reading Polyani: Leadership as ‘Fusion of Power and Purpose’

Yet, the cracks in the current trade order is not just about the collision between domestic and international sources of leadership strategies. It is also a clash between economic (and foreign policy) interests and prevailing ideas and convictions of maintaining the order. Orders are the result of will and capability to construct and maintain effective institutions. It is, however, helpful to relax the sharp separation between interests and ideas. Constructivist do so, by offering an ‘embedded liberalism’ explanation (Ruggie 1982) which focus on the compromise between ideas and interests struck by power-holders in the economy, domestically and internationally, stressing the extent of societal support for trade cooperation.

Facilitative leadership requires domestic demand and international supply, so to speak. Leadership are two sides of the same coin, a convergence of power interests and ideational convictions. Orders are manifestations of power *and* purpose. This interpretation sees a transformation driven by normative reorientations of the dominant states. The apparent retreat of the US from the liberal trading order is a worrisome signal. However, an alternative coalition of normative-aligned government can counterbalance the retreat of the Americans. It is difficult, however. History matters. The evolution of compromised liberalism in trade built on the transatlantic fusion of state power and social purpose of the 1940s, influenced by Keynesian ideas and US liberal foreign policy thinking, and later negotiated updates of that. Everything in the WTO is, from this perspective, about defining the scope of legitimate state interference in the global marketplace. It is not just a substantial norm; it is also an implicit institutional norm, defining the power of the institution itself. Compromised liberalism hinges on the process of hammering out the balance between market liberalization and authority. The two are in constant tension.

Embedded liberalism¹ can be read in different ways. Yet, the essence of the argument is that the liberal trade order rests upon its societal legitimacy. Free trade cannot be separated from the regulation of markets. Market liberalization contains the seeds to its own self-destruction, if left unregulated. It creates a societal pressure for reregulation. Polyani issues a warning about the disembedded market, but he also seem to suggest that it will be balanced by some form of political intervention: "... the positioning of markets within a broader set of social and political rules and cultural understandings that make the market work not only more efficiently but also more equitably, with greater security for market and non-market participants and in tune with a variety of other social purposes..." (Carpuraso and Tarrow 2009: 598).

Translated into here, Polyani informs us that globalization must be regulated by *legitimate* as well as *effective* forms of authority and leadership. This inspired John G. Ruggie to apply the concept to the Bretton Woods institutions (1982, 1995); the General Agreement on Trade and Tariffs (GATT) represented a fusion of international power and domestic societal norms of the dominant states of the immediate post-war era, the US and the UK. Embedded liberalism captured an essential feature of the GATT; that its substantive rules legitimize policy practices intended to cushion the domestic sphere from the destabilizing effects produced by international market liberalization.² The GATT norm was described as 'Smith abroad, Keynes at home'. Moreover, the compromise dictated a state-centered, diplomatic mode of western-dominated multilateral governance. It rested upon a separation of 'the domestic' and 'the international'. The compromise on embedded liberalism, in this interpretation, was never about protectionism. There was about

¹ The notion of embedded liberalism originates from the historical analysis of the 'dual movement' that led to the breakdown of 19th century liberal economic order. By 'dual movement', Karl Polyani (1944) meant that that move towards unregulated market liberalization, whereby the economy was disembedded from its social compound, was accompanied by a political counter-move towards regulating market liberalization.

² [T]he common tendency to view the post-war regimes as liberal regimes, but with lots of cheating on the domestic side, fails to capture the full complexity of the embedded liberalism compromise". Ruggie (1986: 398).

legitimate exceptions, accepted as an overarching social purpose, to trade liberalization. It specifies situations and procedures whereby protectionism is permissible to restrict protectionism. The price for trade liberalization is the tolerance of certain forms of protectionism. Compromised liberalism is about limited trade liberalization. Ruggie focused on the domestic and negotiated origins of the compromise, the US and UK, and excluded other potential sources of a transformed compromised.

What appears missing is the autonomous power and operative design of those institutions hammering out the balance between markets and societies in the liberal order (Mortensen, 2006). Institutional leadership was neglected. Societal domestic support to a compromise, explained by distribution of grains from trade, is one part of the equation. The choice of institutions also builds on frames generated by experiences with multilateral trade, and convictions of what script to follow. Interests, purpose and design are mutually constitutive. The fusion of international power and social purpose within the GATT was until the 1970s complemented by a deliberately weakened design of the GATT institution. This proved unacceptable to the Americans. Effective market access grew into a major concern. From 1970s, the US pushed for a new bargain. From 2003, the US has followed a bilateral path. Yet, the governance design itself of the liberal order must be seen as legitimate. The clash of different national scripts and frames are not just the result of national traditions, but also learning in the GATT/WTO institution.

Both power politics and domestic trade preference of trade is an insufficient explanation of what trade agreements look like. Constructivism can explain why. Trade diplomats do not operate in a vacuum. Calculations of future gains and pains from trade are wracked by uncertainty. Trade diplomats are embedded in intersubjective pre-understandings, worldviews and normative convictions. Uncertainty and complexity complicates the conversion from political intentions to expected effects of different designs. This puts knowledge at the center of the process. Law and by extension, the design of the legal system, offers a simplifying frame for decision makers on complex policy issues (Mortensen 2013). Legal decision making is a sense-making exercise, a subtle form of power, a vehicle of transmitting and consolidating social learning processes. Diplomats employ designs that mirror what is already in place.

“[FTAs] offer continuity with what is in place in a specific region and remind us of the powerful human tendency to mimic what others are doing. [FTAs] are like trees with deep roots in the ground. And they are social products, designed by people who receive their inspiration from, and are influenced by, what surrounds them” (Duina 2010: 113).

The choice of institutional design is about making sense of the world by relying on experience-derived tools of interpretation. Trade diplomats are aware of other free trade agreements, providing them with pre-set instructions about how to solve problems. Scripts are, especially if consistent with the national frames, mimicked by trade diplomats. Institutional bargains are not so much about what is best for trade liberalization or the national interests, but shaped by paths, continuities and expediency. There is no guidebook on how ‘best’ to achieve free trade. For instance, a ‘national legal traditions’ explanation focuses on how legal cultures and

experiences filters through to the diplomats as frames and scripts as diplomats draw on distinct national experiences in trade liberalization in the negotiations themselves. Trade agreements are the end product of specific frames,³ cognitive filters through which diplomats interpret the world and solve problems encountered. Frames work as cognitive filters that determine how trade diplomats approach the problem of market liberalization. Designers of trade agreements also follow distinct scripts,⁴ understood as specific solutions to problems that reflect what is seen as best or most appropriate institutional choice.

If scripts and frames matter, the rational choices of designing an agreement is especially sensitive to different national experiences with free trade. Frames on the legal design have produced two scripts, the interventionist script, i.e., establishment of stronger courts and a minimalist script, i.e., ad hoc tribunals. The civil law frame sees the design choice as a legal problem that calls for a legal solution. Diplomats operate with a pre-designated problem identification of legal harmonization, they automatically identify a need for legal intervention between diverting legal systems. Institutional designers focus on the production of definitional and normative principles as ‘an almost instinctive reaction’ (Duina 2010: 110). Legal interventionist courts is the dominant script. Permanent courts with autonomous powers signal certainty, order and authority. Court-like designs broaden the presence of trade agreement in the eyes of the public, amplify its presence in the public sphere. A more formalized rule of law system reassures a concerned public.

These two scripts stem from different historical experiences. These pre-designated ‘models’ of legal designs in free trade agreements can help explain why a new institutional bargain is so difficult to strike. The Europeans follow their script, constructing more interventionist courts, which makes perfect sense in a European civil law frame. It not only entails a preference for stronger international courts but also a stricter observance of international law, especially respecting the territorial limitations of enforcement provisions. Dialog is preferred over enforcement. The Americans follow their script, pushing for ad hoc tribunals and minimalist legal intervention of international courts. Yet, domestic courts are—in theory—intended to enforce extra-territorial commitments.

The harder American stance on the enforceability, including use of trade sanctions, on environmental and social issues makes sense as ‘leadership’ from this perspective. It is rooted in distinctively different historical experiences with how to solve the clash between different legal systems and traditions. It reflects two different meta-scripts, visible legal activist-minded courts operating in the open, and pragmatic, ad hoc and ‘secretive’ tribunals tackling specific trade problems as they materialize. Yet, the historical experience of free trade is not confined to the national sphere. Past experiences with multilateral trade liberalization also shapes the institutional design choice. The practice of ensuring a balance between

³ ‘Collectively shared and accepted ways of interpreting situations and problems in life. Frames help individuals simplify and make sense of the world’ (Duina 2010: 99).

⁴ ‘Socially available, specific instructions or codes for how to behave in certain situations or respond to particular problems as they arise. Scripts are less about interpreting the world and more about responding to it’. (Duina 2010: 100).

sustainable trade aspirations and respect for the sovereignty norm has defined the past EU position on sustainable trade. The clash of different national scripts and frames are not just the result of national traditions but also learning in the GATT/WTO institution.

3.2 Future Conflicts: Fair Trade, Sustainable Trade

Much of contemporary trade order hinges on the process of determining precisely what the legitimate exception to free trade is. Sustainable trade is precisely about that. Trade governance is the process of hammering out the meaning of ‘the right to regulate’ of the state. It is knowledge intensive, resource demanding and case specific. It builds on the 1947 GATT agreement, article XX. TTIP chapters on regulatory cooperation or investment also refer to that principle and to WTO case law. Governments need to demonstrate that their policies are necessary, impartial and as least trade restrictive possible. Governments who possess the legal and analytical resources not only stand a good chance of winning their cases, they also influence the accumulated body of knowledge on what the law actually means, they tend to take the lead in other negotiations, pre-empt potential problems using these frames, offer solutions and shape the mindset of others to accept their particular framing of the issue at a later point. States use their legal knowledge, the desired legal framings and classifications instrumentally. Other actors also employ legal expertise in the new trade game, NGOs for instance on TTIP. To paraphrase Schaffer (2003, 2006), most of what happens in trade takes place in ‘the shadow of law’.

As mentioned, one of the cornerstones of the WTO is GATT article III, the national treatment principle. Article III (1) establishes a general principle that internal taxes and regulations “should not be applied... so to afford protection to domestic protection”. The national treatment principle is a necessary supplement to the other foundational principle, the most-favored-nation clause (MFN, GATT article I). Any concession granted to a WTO member must be extended to all WTO members. The important exception to national treatment is the ‘general exception’ clause, GATT article XX. GATT art III (4) obliges members to treat ‘like products’ alike in their domestic market. Article XX then determines how to separate legitimate domestic legislation or administrative practices from a disguised trade restriction. The purpose of GATT article XX is clear: disguised trade barriers are illegal, but the WTO agreements also defend the right of states to protect themselves, to set the level of regulation irrespective of what other states do, as long as these do not function as hidden protectionism. The problem is that the WTO agreements do not—and cannot—specify exactly what constitutes a legitimate concern. Fairness cannot be unilaterally determined. Article XX is kept ambiguous. The interpretation of article XX has long been a source of controversy. The precise meaning of article X is lost without extensive references to the GATT/WTO case law on the subject. For instance, it requires trade-related environmental policies to be ‘necessary’ for the policy objective, and not amount to arbitrary and unjustifiable discrimination’. But what does the word ‘necessary’ actually mean? What does ‘arbitrary and unjustifiable discrimination’ look like in reality? In the past, the exact

meaning of the deliberately ambiguous WTO rules is hammered out on a case-by-case basis, but actually producing case law. As it will be shown below, the WTO has been asked to fill out the void on environmental sustainability, but not social sustainability. Institutionalized facilitative leadership builds on institutionalized consensus, reflecting a critical mass of converging societal consensus amongst the power holders in world trade.

3.3 Environmental Sustainability: The Institutional Leadership of the WTO

It was only by the early 1990s it emerged on the agenda, largely because of the infamous Tuna-Dolphin case. The Uruguay Round agreement put ‘sustainable trade’ into the preamble of the WTO agreement. Yet, the article XX texts from 1947 remained unchanged. The word ‘environment’ was not changed. Only through GATT and WTO case law has it acquired a meaning. It is beyond the scope of this paper to outline the legal history of this. Suffice to say here is to emphasize that the issue has today been integrated into WTO law by legal decision-making, panel and appellate body rulings on some of the most dramatic WTO cases such as Shrimp-Turtle, GMOs, asbestos, hormone-treated beef. The WTO did establish a negotiation group on sustainable trade, the Committee of Trade and Environment.

Sustainable trade emerged not because of well-reasoned policy inputs, but because states filed WTO cases against each other on the issue. The WTO had to deal with the problem. Today, negotiations on sustainable trade has had a comeback in the WTO. This is the result of a number of remarkable mixture of policy, law and power. The WTO is the venue for plurilateral negotiations on the liberalization of environmental goods (EGA). However, the WTO is challenged on this by the negotiations on TTIP, TPP and other bilateral agreements, all of which includes chapters on sustainable trade. Sustainability has become a lucrative market, and treated as strategic priority in the struggle for future competitiveness. Climate negotiations can forge a link between trade and climate governance (Pikkerty 2016).

The new trade agreements, launched prior to Trump’s election, were less threatening to the WTO. It is actually supportive to the WTO, for better or worse. A look at what the EU are proposing in the TTIP negotiations on sustainable trade are illuminating. Art 1. reaffirms a commitment to promote sustainable trade in international trade and investment. Art 3. sets out the right to regulate, recognizing the right of each Party to determine its sustainable development policies and priorities, to set and regulate its levels of ... environmental protection. The right to regulate shall ‘be exerted in a manner not inconsistent with ... the environmental agreements’. Art 10. recognizes ‘the value of global environmental governance and rules’, issues a promise to not only strive towards further ratification of Multilateral Environmental Agreements but also acknowledges “that nothing in the Agreement should prevent either Party from adopting or maintaining measures to implement the Multilateral Environmental Agreements to which it is a party, provided that such measures are not applied in a manner that would constitute a means of arbitrary or unjustifiable discrimination between the Parties or a disguised restriction on trade.”

This concluding sentence is taken from WTO law, word by word repeating the chapeaux of GATT article XX.

It is about soft law, rule promotion, fostering cooperation, communication and policy learning. It is not about enforcement.⁵ The CETA text (and, for what it is worth, the proposed TTIP on sustainable trade) is not directly challenging the WTO. TPP had direct enforcement provisions, TTIP reflected the European mode of policy dialog. More importantly, the proposed texts accepted the supremacy of the WTO law. Sustainable trade is encouraged throughout the emerging regime complex by soft governance techniques on a specified list of target issues.⁶ Sustainable trade is not to be enforced by the letter. It also reaffirms the protection of environmental policies derived from WTO law. It addresses the ‘race the bottom’ fear. Art 17. affirms that the parties can uphold their chosen level of protection, recognizing “that it is inappropriate to weaken or reduce the levels of protection afforded in domestic environmental or labor laws to encourage ... trade or investment”, “shall not waive or derogate from, or offer to waive or derogate from, its environmental or labor laws as an encouragement for ... trade or investment”. It accepts everything from WTO case law. States can defend their level of protection, if they demonstrate what is asked by GATT art. XX. By extension, the US and EU cannot enforce this upon other countries. Instead, article 18–20 suggests that transparency, sustainability reviews and CSR measures encourage the spread of sustainable trade practices.

This ‘flaw’ has not gone unnoticed amongst TTIP or TPP critics, however. In a letter from October to the Congress, urging its members to vote no to the TPP, a transnational green policy NGO-coalition also demonstrates the power of legal reasoning in policy debates. TPP’s sustainable trade chapter should “... be judged by whether its provisions are strong enough to have a meaningful impact on the ground in TPP countries and whether the obligations will be enforced”.⁷ They demand obligations to ‘adopt, maintain, and implement its obligations under the

⁵ For instance, art 13 on “sustainable management of forests and trade in forest products “sets out a “... *commitment* to sustainable forest management” which *recognise* “the importance of international rules and agreements in these areas such as such as CITES, UN Forum on Forests or the International Tropical Timber Organisation“. It is a binding treaty text with no mention made of possible sanctions. The US and EU commit themselves to a) “*implement* effective domestic policies and measures to combat illegal logging and related trade, including as appropriate with respect to third countries, and exchange information in this regard; b) *encourage* the use of wood and derived products from sustainably managed forests in their markets and trade thereof...”; c) “identify and *discuss* policies to combat illegal logging and related trade ...”; d) “*exchange* information on trade-related actions taken with respect to third countries ...”; e) “*cooperate* with each other and with third parties to identify capacity-building needs to combat illegal logging and associated trade”; and f) “*cooperate* as appropriate in relevant international fora such as CITES, UN Forum on Forests, International Tropical Timber Council, FAO and the UNECE Committee on Forests and forest-based Industries”.

⁶ The CETA text, and the EU proposal to the TTIP chapter on sustainable trade lists in art 11–15 the different agreements targeted; biological diversity (art 11.), CITES (art 12.), sustainable forest trade (art 13.), sustainable fishing trade (art 14) trade in environmentally sound management of chemicals and waste (art 16.).

⁷ It continues: “Strong obligations with weak or no enforcement would render the chapter meaningless. Our organizations are ... extremely concerned that the provisions agreed ... will not be enforced. The United States has never once brought a trade dispute against another country for failing to live up to its environmental obligations in trade deals even when there has been documented evidence of non-compliance with environmental obligations”.

following specified agreements’, and suggest that CITES or the Montreal Protocol should be supplemented by Whaling Convention, and insert enforceable prohibitions on trade in the covered areas, from illegally sourced timber to trade in illegal fishing.

4 Social Sustainability: Towards Possible Sanctions in the EU?

Social and environmental sustainability has been integrated in the EU trade agreements, reflecting the UN definition. In contrast to environmental sustainability, WTO jurisdiction over social sustainability is extremely limited. This is not a product of negotiations. It derives from past institutional leadership. On social rights, only GATT Article XX e) explicitly put a ban on exports “relating to the products of prison labor”. New demands were put forward on the issue after the establishment of the WTO (1994) but the Singapore meeting (1997) effectively put an end to the social rights agenda in the WTO (Wilkinson 1999). Instead, it referring the issue to the International Labor Organization (ILO) rather than establishing a designated WTO committee. The US enabled harder enforceability of social rights in their trade agreements, from NAFTA to bilateral FTAs, although systematic oversight and enforcement practice on FTA-related social rights provisions never materialized (McBride et al. 2002).

It is no secret that the US more explicitly uses the threat of sanctions in their bilateral trade relations than other trade powers. The US effectively abandoned the multilateral approach in 2003 by igniting a wave of bilateral trade agreements that, among others, including the use of sanctions on non-complying partners. Violations of trade-related sustainability provisions can—in theory—result in trade sanctions in US trade politics. Whereas the US script has been consistently followed, the domestic frame has changed. Demands for fair competition had gained power. The 2016 presidential campaign revealed how powerful these concerns have grown in the US. Both Republicans and Democrats moderated their traditional free trade stance in response to the growing domestic discontent with actual enforcement of sustainability requirements:

“Lack of enforcement by both Democratic and Republican presidents and other flaws with the treaties have allowed countries with weaker laws and standards and widespread labor and environment abuses to undermine treaty provisions, leaving US workers and other interested parties with no recourse” (Warren 2015).

In contrast, the EU have traditionally represented a multilateral approach to the issue. Yet, in response to domestic pressures, the EU is now rethinking their approach.

“While standing for openness and cooperation, the EU cannot be naive in its approach to globalization. There are situations where rules exist but are not respected. Closing the loopholes in global rules and raising standards may take time. In the interim, the EU must have the instruments at its disposal to restore

a level playing field and act decisively against countries or companies that engage in unfair practices. This starts with better enforcement of existing agreements and rules in such areas as trade, labor standards, climate and environment protection.” (European Commission 2017a).

The word ‘enforcement’ is left underspecified by the text. The meaning of enforcement is debated in the European Parliament today. While the EU Commission still negotiates trade agreements, exclusively on behalf of all the EU Member states, the European Parliament’s approval is required for ratification. This includes trade sustainability chapters as confirmed by a recent European Court of Justice ruling (known as Opinion 15/2). The domestic voices demanding a tougher European stance on unfair trade are getting louder, within member states as well as the European Parliament.⁸ In their recent non-paper, the EU Commission (2017b) opens up for the debate on harder enforceability of sustainability requirements in future EU trade agreements. The EU Commission continues to align with the existing EU script: progressive labor and environmental conditionalities are not enhanced by a turn to unilateral, hard enforcement such as in the American trade agreements. Instead, cooperation and promotion of sustainable trade is best achieved by “continuous and long-term engagement with partner countries to create ownership at government and civil society level and inclusive reform processes” (European Commission, 2017b: 4). It continues: “In implementing and enforcing the obligations, the Union recognizes the primary role of international instruments both in terms of standards and compliance mechanisms. ... The EU efforts focus during a first stage on incentivizing the partner country to work with the Union. This is addressed through structured dialogs on sensitive issues, launching joint projects, enhancing interaction with international bodies and setting-up dedicated institutional and civil society structures.

The Commission explains that sustainability requirements are not enforced. Enforcement is subject to state-to-state consultations, expert panel examinations, publicized panel reports, extensive monitoring of the implementation. The EU approach does not include sanctions. Yet, the debate has opened up in Europe. The European Parliament has continuously pushed for more effective implementation. The Commission non-paper is nonetheless acknowledging its critics. It discusses two future models for EU trade agreements. An assertive model and a sanction-based model. The assertive model is consistent with the EU (and WTO) script. The EU continues to work with an integrated sustainability policy but aspires to strengthen its policy by, for instance, improving monitoring of implementation, prioritize quicker responses to allegations of non-compliance, enhancing transparency of complaints, improve precision and priorities of country-specific

⁸ For instance, in their recent comments on the modernization of EU trade agreements (in this case the Chile-EU agreement), the draft of parliamentary International Trade Committee recommended that: “... to ensure that the modernized [EU trade agreements] contains a robust and ambitious [Trade and Sustainable Development chapters] that includes binding and enforceable provisions, subject to dispute settlement mechanisms, with the possibility of imposing sanctions in case of breach; considers that the TSDC should cover, among other things, the parties’ commitment to adopt and maintain in their national laws and regulations the principles enshrined in core ILO conventions and to effectively implement up-to-date ILO instruments” (European Parliament 2017, section x, 13.6.17).

strategies, step up monitoring at government level, and adopting a ‘result-oriented, regular dialog’ with trading partners. These elements of a more assertive EU is in essence quite consistent with the EU script. It is also consistent with the WTO order. It still reflects the postwar consensus on trade in Europe. Sustainability benefits from dialog with internal and external stakeholders and consultations between governments, following a more flexible, differentiated approach, rather than confrontation and hard enforcement.

Yet, the Commission admits that existing trade-related sustainability instruments can be used ‘more assertively, including dispute settlement’ (EU Commission 2017: 5). This category of potential improvements remains unspecified. This is discussed in the latter part of the paper, under the heading of the sanction-based approach. The scenario is that the EU in the future may introduce a dedicated dispute settlement mechanism on sustainability issues, including state-to-state consultations, a panel procedure, a public report, and the possibility to apply sanctions in case of non-compliance. It suggests the possibility of adopting the US script, making it mandatory to enforce domestic labor and environmental laws, and inserting clauses prohibiting the lowering of relevant sustainability standards. This would, admits the Commission, lead to a better and faster handling of stakeholders’ complaints on TSD implementation. Upon reflection, the non-paper remains skeptical towards the actual effectiveness of such an approach.

A sanction-based approach would undermine the current EU strategy of reinforcing the work within the relevant multilateral institutions relating to sustainable development. It would bypass the ILO supervisory mechanisms. It would undermine existing partnerships as well as trade agreements. It would provoke many developing trading partners, who would be inclined to perceive these as ‘confrontational tools’ and thus ‘jeopardize long-term links with partners’. Nonetheless, the Commission also concludes that a shift towards sustainability sanctions could make trading partners “... more willing to strengthen legislation or improve effective implementation of labor and environmental standards if there was a risk of economic consequences. The history of WTO dispute settlement in general shows that such consequences can have an impact. This aspect of effectiveness of sanctions in the context of an FTA would require further analysis.” (EU commission 2017: 8). The domestic sources of EU leadership on sustainable trade have changed. Contrary to the US, the frame of multilateral trade liberalization and the script of cooperative promotion rather than sanctions remain intact. Yet, the policy room for institutional leadership seems to be narrowing in Europe on the issue.

5 Conclusions

The clear definition of legitimacy, authority and procedures in the liberal WTO order, by separating states from non-states in the trade governance, especially in enforcement, is blurring. This could reflect a deeper transformation of the institutional compromise between multilateral, sovereignty and market liberalization. Institutionalized hegemonic leadership, understood as control over a particular site beyond the liberal order, may overshadow institutional facilitative leadership, meaning global,

consensus-based cooperation within the liberal order. It is still much too early to tell whether this is the case in global trade today. The dominant source of leadership appears to have returned to the domestic sphere, marginalizing international courses of leadership. The precise design on the new generation of FTAs is at the time of writing unclear. Cracks are emerging but the complex is also robust. The EU appears firmer orientated towards the liberal WTO order. So far, the enforcement provisions on sustainable trade standards on third parties seems firmly conditioned by the order. The wording of existing EU trade agreements are kept at a WTO-consistent, non-binding format. It accepts the absence of consensus on the issue. It acknowledges the concern.

However, there is a growing crack between the soft, multilateralist-minded approach of the Europeans, shared by most other trading WTO members, and the harder approach of the Americans. Again, two trade agreement scripts appear colliding. While the domestic sources of EU leadership on sustainable trade is transforming, it has not transformed yet, and it is most likely to remain consistent with the past leadership, if European integrations stays on path. The Europeans continue to defend a sovereign-sensitive method in a WTO-consistent manner, compared to the US under President Trump, but the current policy debate points towards serious reconsideration of the EU script, inspired by the US sanction-model of enforceability. A complete order transformation, a turn to forum shifting, remains a potential danger. The turn to unilateralist, even neo-mercantilist, sentiments in especially US trade politics, and subsequent threat of renegotiating of all US trade agreements, may well pit the American script of preferred route, with its domestically controlled hard legal powers up against the multilateralised, court-modeled and more diplomatic-minded European script.

What is increasingly evident is that the learning dynamics of the system is changing. The international sources of leadership appears bypassed in the current trade disorder. Institutional leadership can ensure workable compromises on e.g., legitimate exceptions to trade liberalization, subject to ‘necessity test’ of the GATT article XX that stipulates precise legal requirements of justifying a departure from the international rulebook. Certainty about such legitimate policy exceptions are needed. The domestic sources of leadership cannot be ignored. All states have the right to regulate market liberalization, although not all states are in a position to do so. It is importance to foster mutual learning, enhance transparency and devise solutions to common problems by nurturing institutional leadership. In this case, an important source of leadership on sustainable trade has been WTO case law, ILO monitoring and CSR reporting, signaling precisely what the legitimate exceptions to market liberalization are, to ensure that domestic policy expectations are made compatible with international commitments.

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