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The Production of International Economic Law and the Need for a Cosmopolitan Democracy

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We are writing the constitution of global economy
Renato Ruggerio, Former General Director of the World Trade Organization (WTO)

Introductory Note

This essay is a preliminary effort to assess the way in which the international economic order is being configured. It seeks to begin to understand the mechanisms through which global law in this field is being "produced." The focus of my analysis will be guided by questions such as: Who are the most relevant actors in this process? How are these actors chosen? How do they operate? In view of the large scope of this topic, I have decided to study a specific incident that, in my view, helps to illustrate and focus a debate that—because of its global reach—seems to be excessively abstract.

I. The Problem

In recent times, the debate regarding the benefits and disadvantages of economic globalization has become an issue that not only experts are tackling, but that is also the object of heated disputes between politicians, trade unionists, non-governmental organizations, and the public in general. Among the many issues that have generated this debate, the role played by international organizations such as the World Trade Organization (WTO) or the International Monetary Fund (IMF) in the design of the institutional framework that accompanies globalization processes has been the object of special attention.

There are two basic views regarding the assessment of the way in which the institutional architecture of economic globalization is being designed. On the one hand, there are those who celebrate the result and the mechanisms that have been implemented in recent years. An international network of academics, businessmen, and international officials belonging to the aforementioned international organizations holds this first view. On the other hand, an equally international network of people and groups sees with surprise how economic globalization processes have been detrimental to the ability of states—especially those less developed—to manage their economies with autonomy, in addition to promoting an irrational use of natural resources and contributing to the extinction of ancestral forms of cultural life (which, according to this view, are crushed under the homogenizing weight of globalization).

Once the more relevant actors in the dispute have been identified, it is important to make clear the point that separates them. As we'll see, at the foundation of the debate lies a dispute regarding the democratic legitimacy of those who are making the most important decisions in the design of the governance forms of the emerging new order. This is clear in the accusations made by the "anti-globalization band" (which includes ecologic groups, pro-indigenous rights groups, consumer groups, etc.) about the supposed "imposition" by economic international organizations

of global norms that privilege commercial interests over other values such as environmental protection or labor standards aimed at protecting workers. This accusation is categorically rejected by the official representatives of governments and by the heads of the international organizations that coordinate this kind of meetings. They defend their actions and argue that economic globalization is an undisputable good (ultimately—they argue—it will benefit humanity as a whole because it will promote an international division of labor that will bring about more productivity and, consequently, more economic development and a reduction of poverty) and that the international agreements attacked by the "anti-globalization sectors" are reached by the direct representatives of the participating countries, so the charge of "imposition" loses much of its bite. Moreover—they add—the people who attend international meetings, such as the successive GATT "rounds" that led to the WTO and the following meetings of this organization, are government representatives who, in their majority, have a democratic legitimacy, in contrast to the non-governmental organizations leading street protests, which only represent specific interest groups and not necessarily the national interests at stake, even if the causes they advocate are highly commendable.

In light of these two radically different versions of the generation process of international commerce standards, it is important to assess if the critiques advanced by the anti-globalization groups are well founded. In this essay, I will particularly focus on the second set of objections raised by the anti-globalization sectors; that is to say, the "democratic deficit" affecting the design process of the normative structure accompanying economic globalization. In other words, I am interested in investigating the plausibility of the assertion that there is an "imposition" of international economic rules by the technocratic sectors leading the economies of the participating countries and the economic international organizations that support these processes. In the critics' view these technocratic sectors would be making decisions in the name of millions of people who ultimately will be affected by these processes.

In view of the extension of the problem I want to analyze and the difficulties inherent to this project (especially, if it is undertaken from a peripheral region as ours; that is to say, far away from the places where this type of processes happen), I have decided to study this problem through the analysis of an incident related to the production of the regulatory framework of global economy. The importance of this incident is made clear by the remarks of the former Director of the WTO that I have used as an opening epigraph for this essay, which were made on the occasion of the incident. The case I am referring to is the process whereby the Organization for Economic Cooperation and Development (OECD), which is the international body composed by the most developed countries of the world,[1] tried to promote the adoption of a worldwide agreement on the protection of foreign investment known as the Multilateral Agreement on Investment (MAI). The MAI case is significant because it offers important keys to understanding the complex mechanisms that characterize these processes.

II. The Multilateral Agreement on Investment (MAI)

[1] The member states are: United States, Germany, United Kingdom, France, Japan, Italy, Australia, Canada, Holland, Belgium, Luxembourg, Switzerland, Sweden, New Zealand, Norway, Spain, Portugal, Denmark, Austria, Finland, Ireland, Iceland, Greece, Mexico, Turkey, Poland, Korea, Check Republic, and Hungary.

In 1997, it became publicly known that the OECD was negotiating a multilateral agreement on foreign investment.[2] The MAI is an attempt to establish legislation of global reach providing the basic regulatory structure for foreign investment. The drafters of this initiative deemed it to be a *"necessary complement"* to the rules of international trade.[3] The aim of the MAI was to provide new investors' rights and guarantees that should be respected by the nations receiving the investments. In the drafters' view, the new rules will lead to a heightened role of foreign investment in international economy.

Among the provisions included in the draft of the MAI, there was a section concerning the protection of foreign investors against regulatory measures adopted by host countries causing economic losses. This clause, which established the prohibition of the so-called *"regulatory takings,"* [4] represented a radical change in the traditional concepts of the takings constitutional doctrines of all the countries belonging to the OECD. In fact, as we will see, the incorporation of such an extreme view regarding takings law is really surprising. To be sure, the clause required host countries to compensate foreign corporations negatively affected by state regulations enacted for the protection of the environment, public health, or labor security. In fact, my interest in this topic stemmed from the surprise of seeing in the draft of an agreement for the universal treatment of foreign investment a doctrinal position that has generally been rejected by the countries that drafted the agreement and that specialized literature often deems to be too extreme. This led me to take seriously the possibility that something strange could be happening in the decision-making process of the regulatory framework of global economy. If something strange wasn't happening, how then was it possible that the OECD negotiators reached an agreement adopting a doctrine seen as extreme even in the United States, where the notion of *"regulatory takings"* originated?

My interest was heightened when I noticed that not only something strange was happening, but that the radicalism of the adopted provisions led this project to its complete

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[2] The negotiations leading to the MAI began in May 1995, when the OECD started its negotiations among representatives of the 29 members and a "group of experts" in international trade and investment. The writing of the draft was conducted in secret until 1997, when certain NGOs had access to a 145-page draft written by the negotiating team of the OECD. The NGOs denounced the content as a conspiracy of the rich nations and the international commercial community to *"discuss in private the terms of a global constitution giving huge preeminence to the rights of the investors over the rights of developing countries in issues related to the environment, health, and security."*

[3] The MAI began to be drafted almost at the same time that the WTO started its role as the organization in charge of the application of the rules protecting international trade. The OECD experts that started the negotiations of a multilateral agreement on foreign investment had the view that the MAI was a "necessary complement" to global trade, insofar as the distinction between "trade" and "investment" was being blurred because of the globalization of the economy.

[4] The doctrine known as *"regulatory takings"* basically seeks to extend the logic of the doctrine on regular takings—which demands a compensation from the state when it takes private property; that is to say, when private ownership is transferred to the state—to cases in which the governmental regulation of the use of property has an adverse impact on private property. (A good discussion on the debate on "regulatory takings" may be found in Sax, 1964; Sax, 1971; Michelman, 1971 & 1988; Epstein, 1985; Siegan, 1980; Petersen, 1989; Fischel, 1996; and Coyle, 1993).

failure.[5] To be sure, a consumer protection organization with an anti-globalization stance timely detected the project and led a campaign that was ultimately fatal for this initiative.[6]

The rise and fall of the MAI therefore provides an interesting starting point to understanding how multilateral corporate interests, the discourse of the experts, and the international networks of NGOs combine in the complex world surrounding the making of international economic law.

The structure of this essay is the following: I will first briefly analyze the relationship between economic globalization and law. Then, I will describe the drafting process of the MAI and I will analyze its takings clauses in order to support the argument that these clauses represented a radical innovation in the treatment of the relationship between state-regulation of the economy and private property rights. Finally, I will briefly reflect upon the challenges posed by current processes of global production of law to governance and the possibility of democracy.

III. Globalization and Law

In recent years, the relationship between globalization and public policies has been the object of important academic attention (Reinecke, 1998). People who are interested in this topic usually study the limitations implied by economic interdependency for the domestic design of public policies, especially monetary, fiscal, and labor policies (Bauman, 1999; Gray, 1998; Held, 1995).[7] In spite of the ongoing debate concerning the extent and irreversibility of economic globalization processes and their contribution to the welfare of individuals (Kagan, 1998), few people dispute the fact that economic globalization has constrained the possibilities of action for the domestic design of public policies (Baker, Epstein & Pollin, 1998; Rodrik, 1996).

An important aspect of globalization is law, insofar as public policies are often expressed in legal norms. In any case, it is usually understood that law plays a merely accessory role in these processes. This perspective, therefore, sees the globalization of law as a simple consequence of economic globalization (Shapiro, 1994). According to this view, the rise of an increasingly interdependent worldwide economy might have triggered the development of global laws. The argument goes on to assert that the revolutionary developments in communication and transportation technologies and the possibilities they created for a global production and exchange of goods and services would be the ultimate cause for the globalization of law. This view, however, is incomplete. Although the best communication technologies and the availability of better and cheaper transportation have indeed been necessary conditions for the globalization of the economy, they haven't been sufficient conditions to create a global economy that necessarily demands a set of rules operating as its structural background. In effect, just as

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[5] The MAI failed because an American NGO discovered the existence of the draft. A generalized rejection followed, leading the Council of Ministers of the OECD to announce that it will begin a *"period of evaluation and consultation"* before presenting the draft to the member states for their discussion. A couple of months later, in December 1988, the OECD finally stopped the negotiations of a multilateral agreement on investments.

[6] The organization I am referring to is the American NGO *"Public Citizen"* related to Ralph Nader, a well-known defender of consumer rights in the United States. It is worth noting that this incident signaled the first occasion in which an international coalition of NGOs was successful in blocking an international trade agreement of this dimension.

[7] Among these academics, Bauman's view on the limits imposed by globalization on domestic public policies is the most radical. In his view: "The authorities of the states are not even pretending to be able or willing to guarantee social and economic security to those in their charge; politicians of all tendencies have made clear that in view of the restrictions imposed by competition, efficiency, and flexibility *we can't allow us anymore* to have collective networks of security." Zygmunt Bauman, *In Search of Politics* (Stanford: Stanford University Press, 1999), p. 40.

law was an important precondition for the development of domestic markets (North, 1990; Williamson, 1985), it has also played an essential role in the development of global markets. Instead of being considered a mere consequence of economic globalization, global law, therefore, must be recognized as one of its facilitating elements.

The "constitutive" view of law in the introduction of economic globalization is against the common and mistaken notion that globalization is a self-propelled, inexorable, and probably irreversible tendency generated by forces that, in most cases, are beyond human control (Giddens, 1999).[8] In contrast, I believe that the development of a global economy is far from being irreversible and that it is not the outcome of some sort of natural evolution. Instead, it requires a conscious updating of a structural background of laws and regulations (Gray, 1998). This view of the problem—stemming from the contributions made by Karl Polanyi to economic history a half-century ago—is worthy to be taken into account in times when the inexorability of free market global economy has become a common place for many politicians, public policymakers, and academics. In fact, production and global consumption are now possible thanks to the contributions of a set of legal institutions created in the last decades. These institutions, combined with high development levels of information technologies and improvements in the field of communications, paved the way for the development of an incipient global market.

IV. The Demand of Transnational Corporations for an International Structure of Direct Foreign Investment (DFI)

In the last decades, transnational industries of developed countries have been relocating a growing number of their production processes in developing countries that offer lower labor costs and less regulated business environments. In addition to the relocation of production processes ("outsourcing"), foreign involvement in industries such as mining, forestry, and fishing has reached high levels that have led Direct Foreign Investment (DFI) to become an important factor in the economic future of almost all developing countries.[9] Many people who highlight the advantages of international trade and investment have celebrated this fact: it will result in the creation of a global division of labor, thereby promoting the productivity of all participating countries.[10]

Another element that contributed to higher levels of DFI was the liberalization of trade as such. In effect, the fall of import tariffs and other tariff barriers to trade—a result of four decades of GATT negotiations—substantially contributed to the impressive growth of international trade

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[8] Just as the classic representation of the operation of markets is the *"invisible hand,"* globalization would be—from this point of view—the result of invisible forces beyond human control.

[9] However, the rise in the amount of foreign investment has led to important objections regarding the growing gap between poor and rich nations. This gap is produced by a system where foreign companies raise their profits by paying low salaries to the workers of "host" countries. Others are concerned with the negative impact on the environment produced by growing international trade and investment. In a similar fashion, an awareness has been growing in recent years regarding the dangers of undertaking a "race to the bottom;" that is to say, an offer of worst and worst environmental, health, and labor security standards, which are the product of the competition between poor countries to attract foreign investment through the reduction of those social regulations that have a negative impact on the business environment. In a parallel way, there are also those who pay less attention to the risks of economic globalization, arguing that in spite of all the discourses against globalization almost all countries still have quite autonomous economies. In fact, they show us that even in a country as globalized as the United State, the imports and exports only represent about 12% of the total of the economic product.

[10] *See* Reinicke.

by the end of the 1990s. Global competition was consequently accelerated. In this scenario, more and more companies and industries of OECD countries were forced to consider the relocation of part of its manufacturing production to places with lower labor costs and more lenient environmental standards. The argument is that if corporations of richer countries have the same opportunity to produce the majority of their products in the same place and under the same conditions of their counterparts in the Third World, then they will be able both to reduce their production costs and face the challenges of international competition more satisfactorily. A freer trade regime thus made DFI in developing countries more attractive for OECD countries.

Once the aforementioned technological and political changes led companies of OECD countries to relocate their production processes in other nations, these companies eventually used law to ask for more security and predictability because productive investments—in contrast to short-term capital investments—take a long time. In addition, the huge amounts of capital invested in mining industry, for example, which only produce profits after several years, led foreign investors to put pressure on the host countries to provide higher guarantees. The need for such guarantees arises from the fact that any change in the "rules of the game" that regulate repatriations of profits, labor regulations, environmental standards, etc. represents a threat to these economic interests as real as an unexpected change in the prices of goods or a general economic crisis. However, the difference between this type of fortuitous events and the legal structures governing the rules of foreign investment is that in the latter case it is possible to adopt measures aimed at increasing the degree of predictability. To achieve this goal it is necessary that the new rules become entrenched in the system through legal norms almost impossible to modify such as constitutions or international agreements.

The most important concern of OECD countries investors in developing countries had historically been the possibility of takings or the "nationalization" of their assets. With these experiences in mind (really traumatic for those who experienced them[11]), foreign investors of the developed world investing in developing countries have demanded the existence of constitutional clauses guaranteeing property rights that would protect them against takings without compensation and the enforcement of these clauses by impartial and independent courts.

In the last two decades, however, the risk of "pure and simple" takings has considerably diminished, both because the economic thought of developing world political elites now deems "nationalization" to be an inefficient measure from the economic point of view and because current economic circumstances are forcing developing countries to actively seek for foreign investment (and nationalizations would negatively affect the reception of foreign capital, which would be deterred because of previous cases of nationalized foreign companies).

Although more benign for foreign investment, this new scenario still poses risks for multinational corporations that invest in developing countries. To be sure, there is still a subtler mechanism whereby foreign investors may be partially "expropriated" through governmental regulations aimed at reducing the profits of foreign companies. American specialists have dubbed this phenomenon *"regulatory takings."*

With this more sophisticated form of taking in mind, the expert OECD negotiators included in the draft of the MAI a provision stipulating the duty of host governments to

[11] The so-called "nationalizations" of foreign industries began in the mid-twentieth century and consisted in state authorities taking control of private industries without paying any compensation to their owners or making deferred payments that, in practice, caused huge losses to the former owners. Some of the cases of this phenomenon were the nationalization of American oil companies by the Mexican government in the 1940s and the nationalization of American copper companies by Chilean authorities in the period from 1967 to 1972.

compensate foreign investors whenever governmental regulations would lead to *"regulatory takings."*

V. Property Rights and "Regulatory Takings"

The concept of regulatory taking refers to the expropriation effects of measures aimed at regulating private property. Whereas a traditional government confiscation physically deprives the owner of her ownership, a *regulatory taking* is a de facto expropriation through a regulation that substantially reduces or eliminates the value of property. An example of a regulatory taking that is often mentioned is the case of land-use regulation that prohibits the development of some piece of land in order to protect the environment. This type of regulation may lead to a substantial reduction of the economic value of property. Those who support this view argue that in this type of situations law should treat the regulation as the functional equivalent of confiscation. This argument, however, has often been opposed with the view that, since the rise of modern constitutionalism, the obligation to compensate for government takings is just applicable to confiscations and open takings; that is to say, in cases where public authorities physically deprived an owner of her property.

In 1922, however, the Supreme Court of the United States held for the first time—in Justice Holmes' words—that "if the regulation goes too far" it might become a taking of private property that must be compensated.[12] After the New Deal, however, American courts almost abandoned this doctrine and left the decision to compensate those who had been affected by a regulation to the discretion of federal and state legislatures. In fact, these courts almost never ruled that the regulation at stake had gone "too far" to require the compensation of the owners of the property negatively affected by the regulation.[13]

In spite of the oblivion that covered regulatory takings after the New Deal, since the beginning of the 1980s and the Reagan years this doctrine became the object of much attention in legal and political debates thanks to aggressive campaigns to revive the old *"regulatory takings"* doctrine launched by neo-liberal academics[14] and pro-market organizations such as the Pacific Legal Foundation.[15] These efforts led to two decisions in which the Supreme Court seemed to be

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[12] The case *Pennsylvania Coal Co. v. Mahon*, 260 U.S. 393 (1922), involved a suit of a mining company against the constitutionality of a state statute prohibiting the extraction of coal from the soil of urban areas for public security reasons.

[13] *See* Robert Meltz, Dwight H. Merriam & Richard M. Frank, *The Takings Issue: Constitutional Limits on Land Use Control and Environmental Regulation* (Washington, D.C.: Island Press, 1999). In addition to the United States, other countries have also had to deal with the problem of regulatory takings. For example, the 1980 Chilean Constitution established a strong constitutional protection of property rights, including the duty to compensate in case of regulatory takings. Another interesting case is Canada, which rejected the introduction of the right to private property in its Bill of Rights because of the fear that the new "judicial review" power of the Supreme Court could lead to the preeminence of economic rights over the decisions of democratically elected governmental bodies. Similarly, European countries don't have a protection of property rights against *"regulatory takings."*

[14] The set of academic defenses of the constitutional and philosophical value of demanding compensation from the government in case its regulations of the uses of property have a negative impact on the value of property was initiated by Siegan (1980), and then Epstein (1985), Paul (1987), Macedo (1987), Fischel (1996), among others.

[15] The Pacific Legal Foundation is a non-profit organization located in Sacramento, California, that advocates for the defense of property rights. Since the beginning of the 1980s, this foundation has been involved in the support, financing, and legal advise to owners affected by environmental protection, health, labor security, and rent control regulations.

modifying its half-century-old doctrine on these matters.[16] Despite these decisions—which seemed to suggest that the Court will begin to supervise the expropriation effects of the governmental regulation of property—the reintroduction of administrative takings to American constitutional law never really happened. Defenders of property rights were therefore convinced that it was necessary to amend the US Constitution in order to obligate the government to compensate whenever property-use regulations would substantially reduce the economic value of property. The opportunity for this amendment came in 1994 when the Republicans introduced in Congress their "Contract With America," which included a provision regarding regulatory takings. This provision forced the government to compensate when its regulations reduced in 70% or more the previous value of the affected property. When the "Contract With America" failed, the defenders of property rights kept waiting for the Supreme Court to overrule its doctrine supporting governmental regulation of the uses of private property.[17]

The political context supporting the concept of regulatory takings may be illustrated by an editorial note of a Chilean newspaper—known for its defense of neo-liberal thought—that reveals what is at stake for those who support this concept. *El Mercurio*, a newspaper from Santiago, Chile, published in 1993 the following editorial note relating to the threats to private property in the post-cold war world:

> *"… In our days, the risk to free market posed by Socialism is not in the ghost of takings—for state control of the means of production has lost its popularity everywhere in the world—but in the control of private companies through regulation. In short, Socialism now wants to control private property through the less criticized notion of regulation because it can't anymore deprive owners of the property over their assets."* [18]

Those who advocate the protection of property rights from the political process through the constitutionalization of a right to private property have used different logics in their arguments. Some of them defend the supremacy of private property over democratic decisions with the argument that property is a "natural" and pre-political right granted by God or reason to humanity (Locke, 1975; Nozick, 1974; Epstein, 1985). Theories that see property as a natural right defend its constitutional protection against threats posed by democratic decisions. Others don't view property as a natural right, but they accept the need to constitutionally protect property based on utilitarian arguments. There are also others who—in spite of viewing private property as a natural right—oppose the constitutionalization of property because this strategy might be counterproductive (Span, 1998).

On the other side of the debate on the nature of property rights and their constitutional status, there is a set of theories that attack the notion of a preeminence of property rights over democratic governance. For some people, the right to private property is fundamentally different to other civil and political rights such as free speech or the right not to be tortured. Instead of being a natural and pre-political right, the right to property is deemed to be a conventional

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[16] The decisions of the US Supreme Court that were especially exciting for those who defended property rights in "regulatory takings" cases were the following: First English Evangelical Lutheran Church of Glendale v. Los Angeles County, 482 U.S. 304 (1987); Nollan v. California Coastal Commission, 483 U.S. 825 (1987); and Lucas v. South Carolina Coastal Council, 505 U.S. 1003 (1992).

[17] A point of view that is skeptical of this possibility may be found in the work of Professor Joseph Sax (1995).

[18] *See El Mercurio*, Santiago, Chile, November 10, 1993, p. 3.

mechanism created to advance social progress. Other authors criticize the "untouchable" status of the current distribution of property, while they admit the existence of a general right to have property as a condition for human progress (Waldron, 1988; Nedelsky, 1982). A more radical critique argues that Constitutionalism has historically been the expression of proprietary classes' fear to democracy and, thus, they assert that democracy and private property are inherently in conflict (McPherson, 1979).

Finally, there is a more pragmatic point of view that sees an incompatibility between the notion of regulatory takings, modern industrialized democracies, and a rising demand for regulation in matters such as environmental protection and labor security (Sax, 1995). These commentators note that if the logic of the argument for a strict protection of property rights were to be thoroughly pursued, it would be even possible to reach the absurd conclusion that even taxation is a taking in which the affected person is not compensated! (Especially in the case of progressive taxation.) They argue that this absurd result turns the notion of *regulatory takings* itself into an impossibility.

The debate on the legitimacy of regulatory takings makes evident that the adoption of a position on this matter necessarily involves a reflection about what private property is. According to Carol Rose, the incoherence of the debate on administrative takings is due to the fact that:

> *"…The takings issue masks a logically prior question of some difficulty: that is, in order to say when governmental action 'takes' someone's property, we must have some idea about what rights are included in property in the first place."* [19]

In addition, the complexity of the problems that arise from the regulatory takings issue stems from the fact that while fundamental rights such as the right to free association or religious liberty are not related to the scarcity of resources (it is presumed that the exercise of rights such as freedom of religion or the right to travel is not an obstacle for the exercise of these same rights by others), in the case of property rights scarcity of resources has always meant that these rights are more restricted. The following example, taken from the American experience, may be useful to analyze the tensions involved in this problem.

In the 1970s, the US Congress enacted the Endangered Species Act in order to protect native wildlife. The implementation of this statute constantly requires the enactment of administrative orders prohibiting those uses of the land that may destroy the habitat of endangered species. This type of regulations may produce a sudden (and sometimes total) reduction of the economic value of the land owned by certain people. The affected individuals typically claim that they are the only ones to bear the burden of a social benefit, which, in this case, is the preservation of an endangered species. They add that their land is now being regulated precisely because it was not previously exploited and, therefore, did not play any part in causing the threats to the species now under protection. This—they insist with some bitterness—produces the paradox that in spite of not having contributed to create the problem, they now have to bear the entire burden of keeping alive the endangered species, which, in their view, is highly unfair. Those who defend the notion of regulatory takings think that what would be fair would be to share the cost of the protective measure between all the beneficiaries of the

[19] *See* Carol Rose, "'Takings' and the Practices of Property: Property as Wealth, Property as 'Propriety'," in *Property and Persuasion: Essays on the History, Theory, and Rhetoric of Ownership* (Boulder: Westview Press, 1994), p. 49.

regulation. This would be achieved by taxing every member of the community and by paying compensation to the affected individuals, as it happens with any regular taking. They argue that treating a regulatory taking in identical form to a regular taking is the only way to take property rights seriously.

The problem with this argument, however, is that even if justice issues are deemed to be of the highest importance in regulatory takings cases, an important number of questions will go unanswered. For example, is the government always obligated to compensate—based on justice considerations—those owners negatively affected when the regulation reduces the value of their assets, or when the regulations reduce the value of their private assets, or only when the impact of the regulations reach a threshold—say of 75% of the market value of the regulated property?

This brief summary of the problems implied by the notion of regulatory takings makes evident that this legal field is insidiously complex.

VI. The Provisions of the MAI on "Regulatory Takings"

In the previous section of the essay, I noted the complexity of the problem of regulatory takings. The issue is so complex that the US Supreme Court hasn't been able to come up with a coherent doctrine able to achieve a balance between individual justice and collective rights to self-determination.[20] Despite this complexity, the rules of the MAI on the protection of foreign investors are short and clear: the OECD group adopted an extreme version of the regulatory takings doctrine, so radical that any of the member states has individually applied it. This section of the essay seeks to show the plausibility of this assertion.

In Chapter IV, under the "Investment Protection" Section, the paragraph "Expropriation and Compensation" says the following:

> "Art. 2.1 A *Contracting Party shall not expropriate or nationalize directly or indirectly an investment in its territory of an investor of another Contracting Party or take any measure or measures having equivalent effect (hereinafter referred to as '<u>expropriation'</u>)*[21] *except:*
>
> *a) for a purpose which is in the public interest,*
> *b) on a non discriminatory basis,*
> *c) in accordance with due process of law, and*
> *d) accompanied by payment of prompt, adequate and effective compensation in accordance with Articles 2.2 to 2.5 below*.
>
> Art. 2.2 *Compensation shall be paid without delay*.
>
> Art. 2.3 *Compensation shall be equivalent to the fair market value of the expropriated investment immediately before the expropriation occurred. The fair market value shall not reflect any change in value occurring because the expropriation had become publicly known earlier*.
>
> Art. 2.4 *Compensation shall be fully realizable and freely transferable*.

[20] Andrea Peterson—an expert in property rights—has called this field of law "the most confuse of American constitutional law." *See* Andrea Peterson, ___.
[21] The emphasis is mine.

Art. 2.5 *Compensation shall include interest at a commercial rate established on a market basis for the currency of payment from the date of expropriation until the date of actual payment.*

Art. 2.6 *Due process of law includes, in particular, the right of an investor of a Contracting Party which claims to be affected by expropriation by another Contracting Party to prompt review of its case, including the valuation of its investment and the payment of compensation in accordance with the provisions of this article, by a judicial authority or another competent and independent authority of the latter Contracting Party."*

The definition of expropriation established by the MAI in Article 2.1 was extremely wide, because it included "any measure or measures having equivalent effect" to expropriation. This is precisely the view of those who defend the notion of regulatory takings.

In Chapter VIII, the MAI added to the protection of foreign investment against regulatory takings an additional clause protecting foreign investors against "expropriatory taxation." In effect, under the title "Taxation" this clause required host governments to compensate foreign investors whenever they were taxed with "expropriatory taxes." The clause text was the following:

"1. *Nothing in this Agreement shall apply to taxation measures except as expressly provided in paragraphs 2 to 5 below.*
2. *(Expropriation) shall apply to taxation measures."*

The text of the MAI was accompanied by a document called "Commentary to the MAI Negotiating Text," aimed at clarifying the key concepts established in the agreement. In the section of this document dealing with the clauses on expropriation and compensation, the negotiators repeated (in case there were still doubts) that these clauses covered "*any measure or measures having equivalent effect to expropriation…*" In addition, in the commentaries the negotiators informed that:

"*One delegation proposed additional text on blocking, freezing, sequestration or any similar measures having expropriatory effect. After discussion, it was agreed that these concerns were already addressed: temporary actions, when ended, would result in restitution of property, and, any unlawful aspects of the temporary measure could give rise to damages for breach of other articles, such as Article 1. Should the measures take on a permanent expropriatory character, they would, (i) if lawful, be subject to Article 2..."*

In addition to these rules, the MAI negotiators agreed to extend the protection of foreign investment against regular and regulatory takings to investments constituted before the MAI. In view of the extension of the protection to the property rights of foreign investors established in the MAI, the drafters of the provisions on taxation were forced to add an "interpretive note" that reads as follows:

"*MAI Parties understand that no taxation measures of the Parties effective at the time of signature of the Agreement could be considered expropriatory or having the equivalent effect of expropriation.*"

This caveat, however, was not shared by all delegations, as the Commentaries continue to say: "*Some delegations were not in a position to associate themselves with such a statement.*"

In this section of the essay I have quoted certain clauses of the MAI relating to the issue of expropriation because I think they speak for themselves. The first interesting aspect of these clauses is their radical treatment of the protection of the property rights of foreign investors. In my view, this radicalism is clear in light of the previous sections of the essay, where I shown the reticence of OECD states to accept the compensation for "regulatory takings" and the complexity of this topic.

The second interesting aspect of these clauses is the abrupt equivalence they draw between traditional, physical, taking of private property by the government and *"any measure or measures having equivalent effect."* Any academic or lawyer in the field of American constitutional law, would immediately identify this language as belonging to the regulatory takings doctrine held by those who defend the need to compensate those who are negatively affected by administrative regulations.

The inclusion of taxation as a possible expropriatory measure equivalent to expropriation is also an interesting aspect of these clauses. Constitutions that include this type of rules are indeed very rare. In fact, I have only located something similar in the 1980 Chilean Constitution, which includes a prohibition against "expropriatory taxation."

Finally, another interesting issue is the use of American legal jargon in the drafting of the MAI. This suggests that the key aspects of these clauses were drafted by American lawyers acquainted with the legal debate on regulatory takings in the United States.

In this section of the essay I have shown the radicalism of the proposals included in the MAI. In the following section, I will discuss the implications of this episode for the production of global law.

VII. The Limits of Democratic Governance at a Global Scale

As I explained in the previous section, American defenders of the idea that regulatory takings must be compensated in the same measure that regular takings used both the judicial—which up to now hasn't been effective—and the legislative (through lobbying Republican congressmen who prepared the "Contract With America") paths without any success. A short while after the failure to transform into a statute or constitutional amendment the expropriation clauses of the "Contract With America," this doctrine was included in the draft of an international agreement of global reach—the MAI. This suggests that the same groups that tried to introduce these clauses into American law saw the possibility to use the international spaces of legislative production as an alternative way to achieve in the international context what failed at the domestic level.

In this sense, the MAI episode illustrates a set of phenomena that seem to be configuring the current system of legislative politics formation at a global scale: that is, the preeminent role of experts (evinced in the official presentation of the MAI, which underlined that it had been drafted by "panels of experts" of the OECD), the secret character of the deliberations that precede the drafting of the agreements (also evinced in the case of the MAI, insofar as the OECD

central offices in Paris are not even willing to disclose the names, profession, or nationality of the experts who participated in the drafting of the agreement),[22] the possibility of existence of global lobbying actions, and the possible distortion of all this in the configuration of the rules that are definitively adopted.

The MAI experience also suggests that the rising tendency—predominating in modern democracies—of domestic legislative processes to become discussions between "experts" who negotiate between them in a more or less confidential fashion, without or with very scant participation of the public or its representatives, is adopting a more accentuated shape in legislative processes at a global level. We can also expect that the rise in the number of issues falling under the orbit of global legislation will lead domestic private interests to increasingly lobby the experts in charge of the production of global law. In this sense, the lack of equal access to lobbying that characterizes democracies at the domestic level is heightened in the case of global legislation.

These problems in the global production of law are just an additional instance of the more and more restricted field of democratic governance effectively exercised by the citizens, in an era in which we have accepted the delegation of decision-making power to central banks (in issues regarding the adoption of decisions related to monetary and exchange policies) and constitutional courts (in issues regarding the constitutional legitimacy of regular legislation). In effect, the compounded effect of decisions left to macroeconomists of central banks, to judges, or to the "experts" of international organizations, has substantially reduced the reach of what is actually decided by the citizenry. This leads to the paradox that it is precisely when democracy as a political system has developed its maximum scope—after the so-called "third wave of democratization" (Diamond and Linz, 1996)—the issues that, in practice, are decided by citizens or their representatives are fewer and fewer. Thus, while there are an increasing number of democracies in the world, "democracy" has become less democratic.

Conclusion

The discrepancy between the domestic rules of OECD countries governing the compensation to be paid in expropriation cases and the provisions of the MAI shows the distortion caused by current practices of production of international economic law. It is worth highlighting, more specifically, the dangers involved in trusting the making of these norms to closed groups of experts acting with secrecy.

The MAI experience suggests that the mechanisms that are currently used in the design of the legal framework of economic globalization are subjected to the effects of the so-called "democratic deficit." This phenomenon—which became the focus of much attention in Europe when the bureaucracy of the European Union was criticized for its lack of accountability—seems to be playing a more decisive role in the case of multilateral agreements such as the MAI. The democratic deficits in the production of global law might be possibly due to the fact that the current systems of representation at the international level are inadequate for the contexts in which they have to operate. In effect, although in strict terms the formal mechanisms of representation at the international level are still working (because once the international treaties and agreements are adopted the legislatures still need to ratify what was approved by the heads of state), it is usual that, in practice, governments (especially those of developing countries) present these agreements as a sort of *fait accompli* that cannot be repealed. This is perhaps why

[22] I got this answer from the OECD authorities in Paris.

even though the classic mechanisms of political representation are still currently operating, the rules of the new global economy are seen more and more as the product of secret negotiations conducted by obscure bureaucrats who lack enough democratic legitimacy.

This gives rise to the question whether our current democratic institutions—designed more than two centuries ago—are capable to extend the citizen control that characterizes domestic democracies to the global production of economic rules. To be sure, the fact that classic and modern democratic theories were developed with the existence of autonomous nation-states in mind, which will occasionally join other nations via international treaties, suggests that these theories need to be modified in order to be able to come to terms with a scenario characterized by a constant discussion of multilateral agreements of high technical complexity. In sum, what this is all about is to try to think seriously how to structure the production of global law so that democratic and participatory values have a real expression in that field. If, on the contrary, we leave things as they now are, we might have to confront one of the following problems: a) the production of global economic rules might be eventually deemed to be illegitimate by the majority of the population of the nations affected by these rules; b) the adoption of global economic rules that illegitimately favors the individual interests of entities with bigger economic or cultural capital, or that are more akin to the "epistemic communities" (Haas, 1985) that actually dominate the international economic organizations participating in the production of global legislation; and c) the loss of time and energy of legions of diplomats, academics, and officials of international organizations, in cases when civil society—as it happened with the MAI—notices the adoption of highly controversial agreements that are very difficult to justify and makes them fail.

For these reasons, it seems to me that the MAI episode suggests that the recent calls of political academics such as David Held and Philippe Schmitter to begin the construction of a sort of democratic cosmopolitan rule of law are well founded.

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