GLOBAL TRADE AGREEMENTS:
IMPLICATIONS FOR STATE SOVEREIGNTY

by Suzanne Townsend

Concerns about the ultimate economic benefits of pursing a greatly expanded policy of free trade have been expressed from the start of the negotiations that resulted in the creation of the WTO. The arguments in favor of trade protection for certain domestic commercial interests (such as organized labor, agriculture, and the wood products industry) have been lively and fairly traditional in tone and content. Despite these concerns about the economic benefits, a widespread belief that expanded trade will ultimately be beneficial to the U.S. economy has led to bipartisan support for global trade expansion. Trade negotiations, however, have included little debate about the impact of contemporary trade agreements on state sovereignty, and thus the effect of the agreements on the ability of states to set legislative policy on matters of public interest.

I wrote this article in the hope of fostering debate on this increasingly important issue.

Although only national governments are parties to the various trade agreements, it is understood and intended that the agreements will bind the entire signatory country. In each of the current agreements, the federal government agrees to enforce the provisions of the agreement at the state and local ("subnational") level. Despite repeated promises at the federal level that most state laws would be protected during the negotiation of our trade agreements, the protections afforded state laws (called "reservations" in the agreements) have been described as having a "one-way ratcheting effect." That is, even those state laws that are "reserved" by federal trade negotiators are protected only if they existed before the reservation process. A conflicting state law enacted after the process would enjoy no such protection. A state law that existed and was protected during the negotiation process but that is later amended, is also vulnerable to challenge. In addition, most reservations are time-limited, which means that the protection afforded by the reservation will expire after a certain period, unless the reservation is re-negotiated.

Under our system of federalism, laws and regulations affecting the health, safety, and welfare of the citizens of each state are the province of that state, subject only to the primacy of the federal government in certain areas. The framers of the United States Constitution chose a system of government that recognized the sovereignty of both the individual states and the federal government, in order to balance the power of the government over its citizens. From our country's birth, we have engaged in lively debate about the appropriate balance between the powers of the states and that of the federal government, often using the federal courts as the ultimate arbiters of the sometimes-conflicting interests. The (inevitable and expected) disagreements between the various sovereigns have given us scores of legal decisions defining the balance of this power relationship.

Even though our issues of federalism have been hard fought, and even though they are at the core of our very existence as a country, debate about the impact of contemporary global trade agreements on this balance of power is less than lively. When it has occurred, the debate has too often been both raucous and unfocused. Moreover, despite this relative lack of debate at the state level, based on the recent challenges to state and federal laws under the various trade agreements, it appears that many more state measures may be at risk under our trade agreements than most people realize. Many recent legal challenges demonstrate the breadth of change in the coverage of the agreements—and thus the diversity of laws that are now subject to challenge. (See Brent Foster's article in this issue.)

So, which Oregon laws might be subject to challenge under international trade agreements? Clearly a state law that directly impacts trade by putting a foreign commercial interest at a disadvantage is at risk, absent a specific reservation in the agreement. An example of such a law is ORS 282.210, which requires that all printing, binding, and stationary work performed for Oregon public agencies (subject to certain exceptions) be done in Oregon. However, even state laws that are not directly trade-related, but that do impact foreign trade indirectly, may be subject to challenge. An example is ORS 279.621, which allows Oregon government agencies to give a preference in public contracting to supplies of recycled paper. This statute was not intended to discriminate in favor of, or to specifically assist, Oregon businesses. Rather, the law reflects an Oregon interest in fostering recycling, to reduce the amount of refuse in state landfills. Despite the non-trade intent of this state law, its impact on foreign paper producers brings it under the purview of the expanded trade agreements, and subjects it to the WTO dispute panel precedents which have held that one cannot discriminate against products based on the process by which they are produced. It is this latter category of laws—those that reflect state health, safety, and welfare policy choices in areas other than trade—where the impact of the contemporary trade agreements may be felt most strongly by the states.

The Basis for Suzanne Townsend's Concerns

In the debates over NAFTA and the WTO, some see the issue of the threat to state sovereignty as alarming, others as alarmist. In order to sort through the arguments, it is important to keep in mind that we are in the early stages of WTO and NAFTA dispute settlement precedents, having had only seven years of experience with either forum. The more alarming cases to date have been brought pursuant to NAFTA's Chapter 11, which allows foreign corporations to sue governments directly for actions, laws, or regulations which are "tantamount to expropriation," or impact negatively on profits. (See the cases cited by Brent Foster.)

Conversely, the WTO does not give corporations standing to sue. Any challenges to member countries under the WTO must come from other member countries. The United States Congress as well as several state legislatures and attorneys general have expressed concern about Chapter 11 and its potential replication in the expanded Free Trade Area of the Americas. It is possible, as a result of these concerns, that the FTAA will not allow investors the same rights, but many critics are concerned that corporate advocates for investor rights will prevail. In the meantime, there is no movement by any party to rescind Chapter 11.

Suzanne Townsend cannot foresee whether any of the Oregon statutes that she lists might in fact be challenged by a foreign corporation or government under NAFTA or the WTO—nor can anyone else foresee this. However, the statutes are clearly vulnerable to challenge, in that they do one of the following: 1) discriminate in favor of local products or contractors; 2) discriminate in purchasing on the basis of "process" rather than "product," essentially discriminating against substantially similar products; 3) regulate production or ban imports based on uncertain science (the precautionary principle); or 4) impede imports or exports based on resource preservation considerations which might not be the "least trade-restrictive possible." All of these have been grounds for successful challenges to laws and regulations under the WTO and/or NAFTA.

The following examples of some final WTO dispute settlement decisions might help to clarify these issues:

1995: Venezuela and Brazil successfully challenged the U.S. Clean Air Act provisions regarding the cleanliness of gasoline, because the baseline for foreign suppliers was set by statute while domestic suppliers could use their actual baseline. The EPA argued that it had no records of foreign suppliers' baselines, and thus could not monitor properly. The WTO ruled against the United States, which then altered its regulation accordingly.

1995: The United States challenged Korea's 30-day shelf life requirement for frozen, heat-treated meats as based on unscientific principles. Korea claimed its regulation was necessary to protect public health. The United States claimed that shelf life should be determined by manufacturers. Korea agreed to change its regulation without a final WTO ruling.

1995: The United States successfully challenged Japan's liquor tax law, which imposed lower levels of internal taxes on shochu, a local liquor, than on other distilled spirits. The United States claimed that this discriminated against foreign liquors. The WTO panel and Appellate Body rejected Japan's claim that imported vodka, rum, whiskey, etc. did not compete directly with shochu, as they were "like products" or "substitutable products." Japan changed its tax laws.

1996: The United States successfully challenged the European Union's ban on the import and sale of animals and meat from animals that had been treated with growth hormones. The United States argued that the measures were not based on an assessment of risk, were more trade-restrictive than required to protect human health or life, and were not based on sound scientific principles. The WTO panel and Appellate Body found that the EU measures were inconsistent with the WTO. The Appellate Body found that a member country must demonstrate that the results of a risk assessment "sufficiently warrant or reasonably support" the measure at stake. The United States and the EU have failed to agree on compliance, and the WTO authorized the suspension of U.S. trade concessions to the EU in the amount of $116.8 million per year.

1996: The United States successfully challenged various Canadian laws favoring Canadian periodicals, including postal subsidy rates and an excise tax on split run periodicals (that is, U.S. periodicals containing Canadian advertisements). The WTO's Appellate Body found that the postal subsidy and the excise tax violated national treatment rules (requiring foreign publishing corporations to be treated the same as domestic corporations). Canada complied by repealing the legislation protecting Canadian media.

To date, there have been no rulings under either the WTO or NAFTA which directly impact Oregon statutes. There is no assurance, however, that there will be none in the future. Any foreign country whose corporations seek to do business in our state and knock up against state preferences for local products or "green" products could bring such a challenge under NAFTA. If that were to happen, as Suzanne Townsend points out, the state would not be at the table in the dispute resolution process, it would be represented by the federal government.

Barbara Dudley, guest forum editor

Oregon Laws that may be Impacted by International Trade Agreements

Economic Development

ORS 285A.178 through **285A.186** sets forth a state policy encouraging the development of businesses in certain economically distressed areas of the state. The statutes provide assistance to the self-employed and to start-up businesses (called "microenterprises"), which the state recognizes as the backbone of the Oregon economy. The legislature has instructed the Oregon Economic and Community Development Department (OECDD) to take action to assist these local businesses. This assistance could well be found to be discriminatory against foreign competitors.

ORS 315.507 provides a tax credit to businesses engaged in electronic commerce in certain designated enterprise zones within the state. Again, such credits would have to be applied equally to all competitors regardless of location or employee make-up.

Some states have been active in lobbying federal trade negotiators to protect government subsidies for businesses in economically disadvantaged areas. Although this type of subsidy program has been reserved in recent trade agreement negotiations, it appears that these subsidies are intended to become actionable at some point.

ORS 285A.200 through **285A.218** create Oregon's Credit Enhancement Fund, with the purpose of, among other things, "encourag[ing] the export of goods and services by Oregon businesses in international markets." Under this program, OECDD works with financial institutions to guarantee or otherwise insure or co-insure loans to qualified local businesses. To qualify, an Oregon business must, among other requirements, sell goods or services in markets for which international or national competition exists. This law is similar to the federal export assistance laws which have been successfully challenged by the European Union through the WTO.

ORS 285B.230 through **285B.269** is Oregon's Regional Economic Development Act. The Act creates a Strategic Reserve Fund consisting of public moneys to be used to assist Oregon communities, businesses, and industries that create, expand, and preserve the "principal traded sector industries of Oregon", and encourage diversification and preservation of regional economies.

ORS 526.816 makes it unlawful to export unprocessed timber originating from public lands in Oregon. The WTO appears to prohibit such export controls.

Environmental Health

ORS 468B.130 prohibits the sale or distribution of cleaning agents containing phosphorus in excess of certain amounts, and requires the labeling of such products by percentage of phosphorus by weight. The state legislature adopted these requirements after finding that the presence of large amounts of phosphorus in state waters is a serious pollution and health risk. This could be challenged under either of two standards adopted by WTO dispute resolution panels: as not based on "sound science" or not reflecting the least trade-restrictive measures possible to accomplish the goal.

ORS 468B.485 establishes requirements for financial assurances by ships that transport oil and other hazardous materials in state waters. The legislature intended to protect Oregon's fragile marine environments by requiring ship owners to have sufficient resources to remedy spills and otherwise encourage safety in the shipping of hazardous materials off Oregon's coast.

ORS 459.700 is Oregon's famous "Bottle Bill." The intent of this law is to reduce the amount of solid waste in the state, and thus in our landfills. The law requires that beverage containers sold in Oregon have a refund value of not less than five cents.

For similar reasons, **ORS 459A.780(1)** provides that a state agency many not purchase any product to be used for packaging food if the product is composed of materials that are not either biodegradable or recyclable through an existing recycling program. Furthermore, **ORS 459A.505** requires a minimum recycled content for newsprint sold in the state.

ORS 315.304 and **468.150**, provide a tax credit to firms constructing pollution control facilities in the state.

Environmental Resource Conservation

ORS 498.026 prohibits the import, export, transport, or sale of threatened or endangered species.

ORS 506.109 sets forth a state policy that food fish be managed to provide optimum economic, commercial, recreational, and aesthetic benefits for present and future generations of Oregonians. To this end, the state's Fish and Wildlife Commission is allowed to construct and maintain certain fish hatcheries to rear Coho and Chinook salmon. A fisheries conservation zone is also created for the area within 50 miles of our coastline.

Agricultural and Food Safety

ORS 632.590 requires all unshelled walnuts and filberts sold in the state to be labeled with the name of the state in which the nuts were grown, the grade, brand, and size of the nuts, and the name and address of the grower, dealer, or packer.

ORS 632.490 requires those selling fruits or vegetables in Oregon under a private brand to plainly designate whether the goods are Oregon-grown or packed.

Public Contracting

ORS 279.106 requires certain bidders on public contracts to subcontract a portion of the work to emerging small businesses. This statute evidences a desire that public moneys be shared with small businesses—presumably most of which would be located in Oregon.

ORS 279.835 through **279.840** set up a system of preferences in the awarding of certain public contracts to certain types of sheltered workshops within the state. The statute is intended to encourage self-sufficiency and dignity for the disabled.

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Please review the examples of Oregon laws that might be impacted by trade agreements. This listing of Oregon laws is not meant to be exhaustive, nor is it even clear that a challenge to any of these laws under existing global trade agreements would be successful. However, it is clear that recent challenges by other nations and by commercial investors and foreign corporations have involved laws that are similar in effect to these laws *(see sidebar titled Basis—ed)*. It is also clear that current federal trade policy aims to broaden the coverage and scope of our global trade agreements. (A good source for details on cases brought under the WTO is the Government Accounting Office's Web site at www.gao.gov)

Although states have witnessed sizeable increases in centralized federal control over many health and safety issues within the past century, we are still used to having our say in most matters affecting our welfare, health, and safety. We are knowledgeable about the mechanisms for influencing public policy on the federal level in matters concerning domestic policy. We are also used to having significant local control over our own natural resources and the quality and content of our lives within our state's geographic boundaries.

Policy decisions in areas such as water quality, water resource allocation, land use planning, local zoning, recycling, wildlife preservation, health care planning, use of state funds, state tax policy, and state government contracting have historically been debated and decided by our local legislators, or have been the subject of our initiative process. We do not now routinely consider the implications of our local policy choices on the wider stage of cross-border commerce. Nor are we widely conversant with the political and legal mechanisms by which state interests can be expressed and protected in the contemporary global context.

At the state level, our relative inexperience in the realm of trade policy negotiations hampers our ability to be heard. Not only are the states absent from the negotiating table during these trade negotiations, they also have no standing before the dispute resolution bodies created by the trade agreements. Indeed, although the separate quasi-judicial dispute resolution systems and other dispute resolution processes established under the various trade agreements allow other nations, and also foreign corporations and investors, to bring challenges to state laws and regulations, states themselves are not parties to disputes, even when their own laws are challenged. Although decisions by arbitration panels created under the auspices of the trade agreements will not result in the automatic overturning of any state (or federal) law, states have a clear interest in the proceedings. Adverse decisions put strong pressure on nations to change laws and regulations found to conflict with a trade agreement, and may also result in significant monetary damage claims.

When viewed from the perspective of the states, the current situation may represent nothing less than a radical shift in the balance of power, both between the federal and state governments and between the states and private commercial and investment interests. In essence, are the states de facto agreeing to give up governmental regulatory authority in certain areas, in the interest of increasing market access and profitability? Will contemporary trade agreements adversely impact the ability of states to govern in those areas that, under our system of federalism, have historically been the province of the states? What are the risks inherent in having Oregon's ability to legislate on matters of the health, safety, and welfare of our citizens subjected to negotiations to which we are not a party? Is it a necessary outcome of the trade agreements that state laws protecting health, safety, and the environment are sacrificed? Will state interests be adequately protected, when a challenge to a state law is made in tribunals or courts in which states have no legal standing? What role, if any, should states have in future trade agreement negotiations? What types of governmental authority are we willing to give up in order to maximize business profits?

Oregon is a state in financial crisis. We increasingly tie our economic future to expanded global export capacity and simultaneously to attracting tourism based on the beauty of our natural resources. We are also historically a state with strong opinions about controlling our own destiny and the quality of our lives, as evidenced by our leadership in creating the initiative process and the referendum, by the groundbreaking statutes that declared our beaches to be public spaces, by our strong land use laws, and by our willingness to step to the forefront of the ethical debate concerning quality of life issues, with the Death with Dignity Act and the Oregon Health Plan.

As Oregonians, we have a substantial interest in understanding the potential impact of international trade agreements on our ability to foster and encourage the growth of our local business, to protect our health and safety, to protect our natural resources and generally our ability to make critical ethical decisions that impact our quality of life. I wrote this article in the hope of fostering debate on this increasingly important issue.

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