

Reappraisal

Trading Away Free Trade

by Fred L. Smith, Jr.

The creation of the World Trade Organization was supposed to be a landmark victory for free trade. But was it?

The General Agreement on Tariffs and Trade has lowered the world's tariff barriers fairly well. Its proponents — including the Cato Institute and other libertarian groups — argue that the latest modification to GATT, the World Trade Organization, will advance free trade even further.

So does the Clinton administration, which negotiated the final agreement, and so have most large businesses. It is opposed by a handful of populists like Ralph Nader and Pat Buchanan, with environmental and labor groups withholding support until further "protections" are added.

The WTO builds on GATT's base, adding trade in services and intellectual property to the trade in goods already covered by GATT. It is being sold as a global equivalent of the interstate commerce clause of the U.S. Constitution, as a guarantee of the right to buy and sell goods throughout the world. But it may prove instead to be more like the Interstate Commerce Commission — a tool for the cartelization of economic activity, the exploitation of consumers, and the suppression of economic liberty.

Revamping GATT

Free trade needn't involve foreign entanglements. It only requires removing a nation's own barriers to international exchange. But protectionism is a powerful force, and few legislators are eager to confront special interests out to escape foreign competition. So they pander to producers whose goods are blocked from other countries' markets.

Usually, they try to open those markets with "retaliation": "if you don't open your borders to my goods, I'll block your goods from my markets." This strategy rarely works even on its own terms; as Jim Powell has pointed out, "it is hard to find a single significant case in which trade retaliation or retaliatory threats have forced open a foreign market" ("Why Trade Retaliation Closes Markets and Impoverishes People," *Cato Policy Analysis* #143).

GATT also relies on trade retaliation. Nations bring disputes before GATT, and a panel is convened to judge the merits of the charges. If a country is found guilty of blocking trade, the offended nation is entitled to impose penalties against the offender's imports. Despite its authorization of this dubious practice, GATT seems to have worked fairly well: tariffs have been gradually reduced and world trade has increased. It is important to remember, though, that the system was never intended to promote free trade *per se*. Lower tariffs and increased trade may have occurred despite GATT as much as because of it.

At the same time, lower tariffs have increased the importance of other

forms of protectionism. These new restraints are inherently more difficult to resolve — or detect. Unmodified cars are difficult to sell in England or Japan, where people drive on the left side of the road. Is this a trade barrier? Aggressive exporters convinced of the superiority of their products and selling abilities are too quick to see non-tariff barriers where brand loyalty, price or quality differences, lack of repair facilities, or already well-established trading patterns are to blame for their problems. To hear some firms tell it, *any* lack of sales is a result of foreign protectionism.

Will the WTO erase real impediments to free trade, or will it pander to fears of pantomime protectionism? You have to wonder.

For one thing, by widening the range of products covered by GATT, the WTO widens the scope of cross-retaliation against products not involved in the original dispute. Thus, the WTO sharpens the sting of trade sanctions by allowing governments to punish each other in ways that cause the most pain, dragging unrelated businesses into a trade dispute: an American software firm, for example,

might be punished in retaliation for an American agricultural firm selling rice too cheaply in Japan.

Clinton's negotiators, not known for their staunch free trade principles, incorporated some troublesome aspects of U.S. anti-dumping and countervailing duties laws into the GATT agreement, legitimizing the protectionist rules of the U.S. International Trade Commission and the Department of Commerce. European nations, in turn, insisted on explicitly defining their industrial-policy subsidies as acceptable trading practices. The Clintonites accepted these changes, which allow them to expand the domestic subsidies *they* wish to pursue. Combined with the European demand to allow export rebates for energy taxes, GATT's subsidy provisions could encourage European-style industrial policy in the U.S. and other nations.

Because the Uruguay Round of international tariff-reduction negotiations must be ratified as a trade agreement, the WTO will enjoy an enhanced status as its global enforcement arm. The voting rules of this bureaucracy are different from those of the old GATT, where decisions were made by consensus and voting procedures were rarely invoked. Like the United Nations General Assembly, every nation, regardless of size, will have an equal vote in the WTO. Larger nations will receive no Security Council-style veto, nor will they benefit from weighted voting, as in the World Bank and the International Monetary Fund. Moreover, unlike the old GATT, the WTO envisions incremental, one-at-a-time modifications in trade rules, each voted on separately. GATT rounds, by contrast, were package deals — complex sets of negotiated tariff reductions across a wide array of goods traded by many nations.

The United States found it much easier to close unnecessary military bases with a GATT-style package deal than with the WTO's incremental approach. Will similar incentive problems hamper efforts to reduce trade barriers?

Moreover, the WTO rules encourage "public participation," ensuring a change in the forces influencing future trade disputes. Mickey Kantor's claims that these rules will make it easier for citizens' interests to be represented are not to be believed. In the U.S., "public

participation" has become a code phrase for granting extraordinary powers to narrow pressure groups. The all-too-likely beneficiaries of the public-participation provisions will be the "progressive" activist groups that have done so much to politicize the U.S. economy.

One danger inherent in an unweighted, veto-free voting system is that such groups could work with foreign protectionists to advance the ideologues' domestic agendas. For example, a German firm might argue that America's lower rates of recycling or higher rates of energy consumption are "non-sustainable," and thus constitute an un-

Will the WTO pander to fears of pantomime protectionism?

fair trading practice. The EC has already effectively excluded Spanish beer from German markets by requiring that all beer be sold in reusable bottles.

Deceptive Greenspeak

The Clinton Administration, supported by France and other nations, has pushed for a commission to consider how the WTO system should be modified to advance "fair," "sustainable," and "socially just" trade. The dominant multinational corporations, non-governmental organizations (NGOs), environmental activist groups, and government elites seem in general agreement that a more tightly managed world trading system is preferable to a free one. In this context, one has to wonder whether the WTO will advance or retard economic liberty.

The WTO's preamble already incorporates hortatory requirements that trade be compatible with government-defined environmental goals and that it encourage "sustainable development." America's experience with environmental laws provide good reasons to take such rhetoric seriously. The 1972 Clean Water Act gives the federal government regulatory authority over the navigable waters of the United States. Who could have dreamt that "navigable waters" would one day be interpreted so broadly as to allow the EPA and Army Corps

of Engineers to impose land use controls on hundreds of millions of acres of private property under the guise of protecting "wetlands"?

Radical reinterpretations of such clear language have characterized most domestic environmental statutes — the Endangered Species Act, various hazardous waste laws, recycling mandates, etc. Why should we believe that free marketeers will be any better at stopping encroachments on "clear language" in the future than they have been in the past?

Our past experience with multinational agreements is cause for pessimism. When George Bush signed the Global Climate Convention in Rio, he assured us that it would be non-binding. Now the Clinton-Gore administration has informed us that it *is* binding, committing the U.S. to reducing carbon dioxide emissions to 1990 levels by the year 2000. This administration has also suggested that the treaty may be used to raise fuel economy standards, extending a deadly regulation that already causes thousands of highway fatalities each year. George Bush also signed Agenda 21, the Earth Summit's blueprint for "sustainable development" policies, including new restrictions on global commerce rationalized on environmental grounds. The U.N. Development Programme proposes a global trade levy as an initial means to that end.

The WTO's preamble, along with Keynesian goals of "effective demand" and "full employment," affirms the need for a greening of trade:

- It asserts the importance of "allowing for the optimal use of the world's resources in accordance with the objective of sustainable development, seeking both to protect and preserve the environment and enhance the means for doing so. . . ."
- WTO nations are committed to "harmonize" their technical regulations and sanitary standards. Provision is made for nations to adopt measures different from international standards, but only if they are more stringent. Downward harmonization is officially discouraged, though not prohibited — yet.
- The dispute settlement under-

standing allows nations and arbitration panels to seek scientific and technical advice from any individual or organization. NGOs will enjoy more "public participation" rights under these procedures.

- The Clinton administration fought to establish a WTO Committee on Trade and the Environment at the insistence of Sen. Max Baucus (D-MT) and other congressional environmentalists. It will develop modifications to WTO policies in order to support "sustainable development," including economic instruments, pollution charges and environmental taxes, compulsory recycling, regulation of processes and production methods, packaging and labelling requirements, and "public participation" rights. It may review any trade-related issue, including carbon taxes, levies on fossil fuels, and transportation restrictions.
- Thanks to French and American pressure, a general committee will address how the WTO can ensure "basic rights" for workers — i.e., labor laws that produce unemployment.

Some analysts assert that such managed trade policies merely represent a desirable extension of the Hayekian rule of law. That is nonsense. Hayek saw no virtue in harmonization or standardization for its own sake. He reminded us that legislation works best where customs, values, and language are already shared. This world is not such a place. Attempting to impose a "rule of law" on the international trading system via the WTO, or any other centralized organization, will be a com-

plex and most likely ill-fated enterprise. Uniform rules that evolve through voluntary arrangements are beneficial; those imposed by some exogenous authority are not.

The New World Trading Order

The WTO's political centralization could come at the expense of our decentralized federal-state-local relationships. Writing in *Commentary*, Jeremy Rabkin effectively describes what is at stake:

Sovereignty is not a matter of legal formalities . . . [The] erosion of sovereignty entails a blurring of the lines of accountability. . . . [T]he internationalization of our domestic policy disputes adds one more — and potentially much larger and more intricate — layer of technical confusion between public preferences and the excuses of politicians not to respond to them. It makes government that much more obscure, remote, and inaccessible to ordinary citizens.

Consider our disastrous experiences with other global bureaucracies. GATT worked fairly well under its consensus rules, but it is an exception. More common is the phenomenal mischief-making of the World Bank and IMF, which have repeatedly destroyed economies, bailed out state socialism, and — despite their newfound environmentalist rhetoric — wreaked enormous ecological damage. Recent internal audits of the World Bank revealed a 37.5% failure rate on its lending projects. Few IMF loan recipients have become economically self-sufficient, and IMF conditionality arrangements have led to increased taxation, "balanced" trade policies, and other destructive statist programs.

Institutions are shaped by the incentives they create. GATT's focus on reducing tariffs encouraged a pro-trade bureaucracy. By contrast, the U.S. International Trade Commission, the Commerce Department, and the U.S. Trade Representative are charged with ensuring "fair" trade; for that reason,

they have never been proponents of free trade, even under the nominally anti-protectionist Reagan administration

At the WTO, U.S. economic interests are all too likely to promote a quota approach to trade policy, to find "unfairness" in any lack of market penetration, to see the use of a language other than English as a non-tariff barrier. And U.S. ideological interests are all too likely to use the WTO to promote a "social trade" agenda.

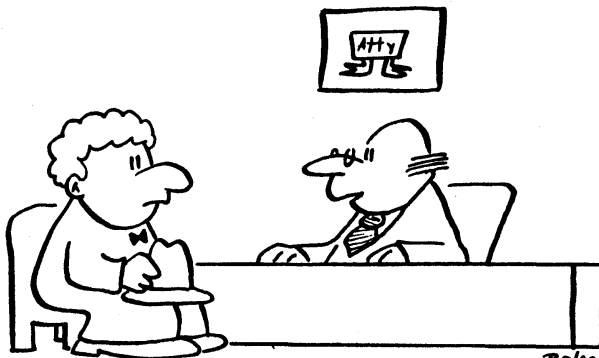
Exploiting the Third World

Some WTO proponents have seen virtue in the power the one-nation-one-vote system gives to smaller nations, arguing that the Third World has a strong stake in free trade and will counterbalance the regulatory demands of the U.S., Europe, and Japan. But experience with existing environmental treaties suggests they are wrong.

The International Whaling Commission was intended to ensure sustainable harvesting of whales, but has been transformed into an anti-development, pro-animal-rights statute. Even Norway's Prime Minister Gro Harlem Brundtland, the Joan of Arc of the Earth Summit, cannot control this process; recently, she charged the Clinton-Gore administration with caring more about whales than about people. Yet few of the world's nations care enough to oppose the movement to ban whaling — and those that do were outvoted by the NGO-influenced majority of nations.

Much of the Third World supported the Basel Convention, an agreement based on the premise that trade in hazardous waste services should be avoided wherever possible. Likewise, developing countries signed on to the Convention on Trade in Endangered Species (CITES), pushed by European and American environmental establishment groups seeking publicity and funding. The effect of CITES is to punish nations with sound conservation programs. A handful of African nations are beginning to have second thoughts about CITES, but so far too few to yet have an impact.

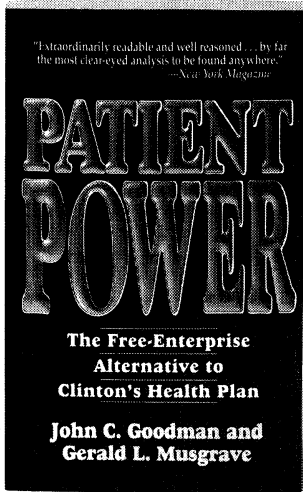
These experiences illustrate that developing nations are an ineffective force for free trade. Worse, they demonstrate that Third World elites have no compunction against betraying



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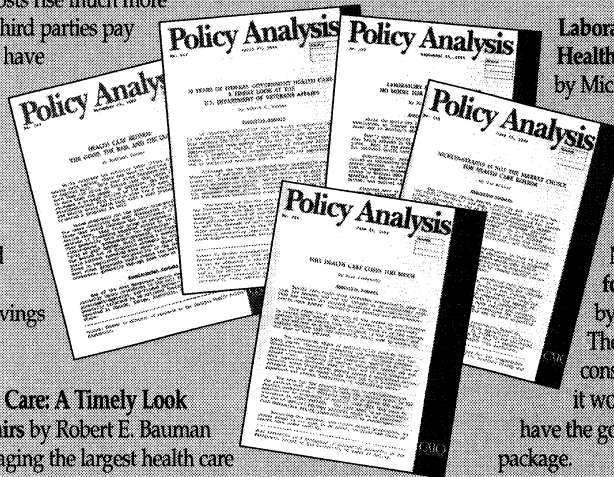
system in the nation should caution us about the dangers of turning more health care over to government management.

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The reforms implemented by Hawaii, Oregon, New York, and other states should not be a model for national health care reform.

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their own people for personal gain. Foreign aid cannot compensate the world for the damage done by protectionism and regulation, but it can buy a lot of environmentalist Uncle Toms ready to sell their fellow citizens down the river. Will the Third World be crucified on a cross of green?

Global Cartels

The late nineteenth century was the era of robber-baron capitalism and rapid economic growth. For the first time, many firms were operating at a national level. The interstate commerce clause prevented Balkanization, while the lack of any federal political entity able to protect a specific firm, to "regu-

late" commerce, made cartelization impossible. Competition was inevitable and the nation prospered.

Neither business nor politicians nor the "public interest" community were happy about this. In the late nineteenth century, economic interests (railroads out to suppress competition) and ideological interests (anti-market Progressives) pushed for a federal body able to restrain competition. Together, this Baptist-Bootlegger coalition succeeded in creating the Interstate Commerce Commission, which suppressed transportation competition for almost 100 years under the guise of harmonizing and ordering the patchwork of state and local regulatory regimes.

In the late twentieth century, firms operate in a global economy. Without a global political entity to restrain trade, to "harmonize" regulations, to create a "level playing field," special interests and ideological groups lack the means of restricting competition. The value of trade and the mobility of capital create the functional equivalent of the interstate commerce clause that protected internal trade in the United States before the railroads and Progressives managed to establish the ICC.

Today, economic interests (major multinational corporations) stressed by global competition join with ideological interests (a powerful environmental movement) to create the global equivalent of the Interstate Commerce Commission — an agency that could restrain trade to ensure that it is "sustainable."

None of the other Bretton Woods institutions — the World Bank, the IMF, the old GATT — can play this global cartelization role. Nor could the U.N. But the WTO might.

Like NAFTA, the WTO's merits will be determined by seemingly marginal details — in particular, the actions of its Committee on Trade and the Environment. Disturbing trends have already begun to emerge from NAFTA's side agreements. The Mexican operations of General Electric and Honeywell have been charged with violating NAFTA's labor laws, and both companies are now under investigation. Even if no formal disciplinary action is taken, these companies will have been forced to spend substantial sums in their defense, setting a grim example for other businesses. Mexico has already been pressured into adopting U.S.-style laws regarding food inspection and the transportation of hazardous wastes. And U.S. firms are being pressured to comply with U.S. toxic release inventory laws in Mexico, even though no law requires this as such.

If NAFTA could already do so much damage, do we really have nothing to fear from the WTO?

But even without these complexities, the WTO deserves scrutiny. It is a GATT with teeth, and those teeth can enable it to discipline protectionism. They can also enable it to enforce protectionism more effectively than ever before. □

Academic Style¹

An interesting question which has received comparatively little attention in the academic literature is whether somebody prosecuted for tax evasion can be said to be prosecuted in any meaningful sense of the word.² Indeed, the student of state persecution is faced with a difficult task because so little research has been done, and the literature on this topic is polemical rather than analytical, and must therefore be treated with caution.³

Professor John Kenneth Galbraith (Galbraith [1954], p. 295), in a carefully-reasoned argument, explicitly recognizes that "The more comprehensive the tax system — the fewer the loopholes — the better it serves both equality and stabilization."⁴ Although it is not clear what Galbraith means by "loopholes"⁵ (and although I am not a brain surgeon), it appears that broad historical trends support his argument.^{6,7} But the reader must be careful (Himself [1996]) in interpreting this evidence.⁸ Obviously, more research is needed before a definitive conclusion can be drawn.⁹ —*Pierre Lemieux*¹⁰

Notes:

1. I would like to thank my wife, Nancy, and my secretary, Pam, without the support of whom (including the latter's old IBM Selectric) this article could not have been written. I am also grateful to an anonymous referee from this journal. Of course, any remaining error is entirely mine. NSF Grant #192-370-568-5666780.
2. I am not concerned here with the moral aspects of the question. On this, see Rawls [1971].
3. A good example is, of course, the little book by Frank Chodorov [1954], where the author argues in a somewhat anecdotal fashion that the income tax breeds state persecution.
4. Emphasis mine.
5. Recent reports (see the *New York Times*, June 3, 1994) of trouble with "potholes" may provide a clue.
6. See also Zauberman ([1967], p. 291): "... the Soviet model was designed in the Central Economic Mathematical Institute of the Soviet Academy of Sciences (denoted thereafter as 'Ts'). Neither its numerical solutions nor its fate have been revealed. Nevertheless, it deserves our attention as an important stage in the history of formalized planning techniques."
7. If I understand Galbraith's argument correctly, it implies that the tax evader is a criminal.
8. I choose to avoid here the argument raised by Lysander Spooner (Spooner [1870]) to the effect that resisting robbery is legitimate.
9. Perhaps a little anecdote will help the reader understand the main thrust of the argument here. A friend of mine who was mugged said that, on the other hand, he has never been prosecuted for tax evasion.
10. Not the author. Article quoted from the *Old England Journal of Medicine*.

Sources:

- Chodorov, Frank [1954], *The Income Tax, Root of All Evil* (Old Greenwich: Devin-Aldair).
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