within the EEC to tolerate national "grey area trade restrictions" by individual EEC member states (e.g. the long-standing VERs of England, France and Italy limiting the market share of Japanese automobiles in these countries) and to reinterpret the temporary safeguard clause of Article 115 of the EEC Treaty in a way allowing the continued maintenance of national import quotas and supplementary trade barriers within the EEC.180

THIRD PART: CONSTITUTIONAL FUNCTIONS OF LIBERAL INTERNATIONAL ECONOMIC RULES

"Perhaps the most difficult question to determine is how much to decide by rule and how much to leave to discretion." "It is an advantage, and not a disadvantage, of the scheme that it leaves the member States to abandon that licence to promote indiscipline, disorder and bad-neighbourliness which, to the general disadvantage, they have been free to exercise hitherto".

J.M. Keynes1

Here is an attempt to use what we have learnt from modern experience and modern analysis, not to defuse, but to implement the wisdom of Adam Smith... They (the international agreements) aim, above all, at the restoration of multilateral trade... The bias of the policies before us is against better and every kind of discriminatory practice. The separate economic blocs and the friction and loss of friendship they must bring with them are expedients to which one may be driven in a hostile world, where trade has ceased over wide areas to be co-operative and peaceful and where are forgotten the healthy rules of mutual advantage and equal treatment. But it is surely crazy to prefer that".

J.M. Keynes2

180 See the recent "Test-judgment" by the EC Court of Justice relating to Article 115 (quoted above in note 61) and, in regards to the toleration of national VERs, the literature quoted above in note 53 as well as: M.C.E.J. Bromley, A Legal Analysis of Protective Measures Affecting Japanese Imports into the European Community, in: E. Volker (ed.), Protectionism and the European Community, second edition 1987, pp. 94 ff.


VII. CONSTITUTIONAL FUNCTIONS OF LIBERAL INTERNATIONAL TRADE AND MONETARY RULES

1. Notion and Functions of "Constitutional Rules"

A) The Reason of Rules

The international division of labour among today more than 170 states consists of millions of constantly changing relations between producers, investors, researchers, importers, exporters, consumers and government officials. The particular facts and concrete events which the individual economic agents encounter in their daily pursuits (e.g., a new discovery) and which affect the course of the international division of labour, cannot be known to any individual or government in its entirety. This irremediable ignorance of everyone of most of the particular facts which determine the actions of all the other participants in the international division of labour, can be reduced only by reliance on the information supplied by rules of conduct and market prices which enable individuals to form reasonably correct expectations and induce the international division of labour to constantly adapt itself to the continuous change.

According to F.A. Hayek, most of the rules of conduct governing individual actions, and most of the institutions which arose out of this regularity, are adaptations to this fragmentation and individual limitation of our knowledge. Yet, "it is the utilization of much more knowledge than anyone can possess, and therefore the fact that each moves within a coherent structure most of whose determinants are unknown to him, that constitutes the distinctive feature of all advanced civilizations." According to Hayek's theory of "spontaneous order", many rules of conduct have developed through a process of "learning from experience" and have prevailed because the regularity of certain actions made a group of men successful. Like the spontaneous evolution of human languages or animal societies into complex orders that were not deliberately created, many rules and institutions of private commercial law (such as recognition and transferability of property rights, "pacta sunt servanda") historically evolved and survived because they brought benefits to those groups of people who adopted them. International commerce during more than two thousand years has given rise to systems of

private commercial law regulating private commercial transactions with much more complex structures than public international trade law regulating the conduct of governmental trade policies.

The need to distinguish spontaneously grown, self-generating "orders" from deliberately constructed "organizations" has been emphasized already (above chapter III.1). Wherever people regularly interact - be it in the polity, in the economy, in road traffic or in social games - rules and procedures of general application are necessary for coordinating the autonomous activities. Spontaneous orders emerge from rule-oriented free actions and are based upon rules protecting and coordinating the autonomous exercise of individual liberties (or "sovereignities") without prescribing specific results or purposes. Organizations are deliberately created to serve a particular purpose and are based upon rules for the performance of assigned tasks so as to achieve the predetermined objectives. Spontaneous orders based upon individual liberty enable the use of more individual knowledge of local events, individual experimentation (based on "trial and error") and spontaneous, individual adjustment and are therefore capable of much greater complexity than any planned organization, because they draw upon more facts than any central authority can know and continuously adapt to a large number of events unknown in their totality to anyone. Just as languages may be spoken without conscious knowledge of their grammar rules, the "regularity" of national and international economic orders may be due to rules explicitly known or unknown to those behaving in accordance with the rules. A particular feature of legally binding rules of conduct is that their content can be, and often has been, laid down or modified by law-making agencies and their applicability and meaning in a concrete situation can be determined through ordered procedures and law-applying agencies.

B) Need for and Functions of Constitutional Rules

Freedom and "sovereignty" may be used in a variety of ways not only for the good but also for the bad. Just as life in a society without rules would tend to be "poor, nasty, brutish and short", as Thomas Hobbes pointed out in his

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4 That complexity needs freedom is one of F.Hayek's main arguments in favor of a rule-guided liberal order based upon individual liberty, see Volume 1 of F.Hayek's Law, Legislation and Liberty (above note 3).
5 See also E.J. Meinecke, Regelführung und Rechtsschutz in Marktwirtschaftlichen Ordnungen, 1953, p.6.
"Leviathan" (1651), people and societies all over the world have found it necessary to establish or recognize government organizations in order to protect the equal rights of people and prevent citizens from breaking the rules. The "constitutional rules", by constituting and limiting government powers so that the holders of government powers remain limited and governed by long-term rules of a higher rank, provide a sort of "meta-rules": They contain the "constitutional choice" of the fundamental "rules of the game", determin the long-term institutions of a political system and provide the legal standards against which the "postconstitutional choices" and current processes within the constitutional rules are to be judged. 6 The distinctive contribution of American constitutional law was to assert the supremacy of individual rights over governmental powers and, as spelled out in the Declaration of Independence, "that to secure these rights, governments are instituted among men, deriving their just powers from the consent of the governed". The need for constitutional rules thus derives from the insight that the short-term identifiable self-interests of both private individuals and government officials often come into conflict and that the current social processes do not lead to optimal results unless they are constrained by long-term rules and, if necessary, their collective enforcement. The prospective, general and permanent nature of constitutional rules acts as an incentive for individuals to concentrate on their long-term common interests (the "public interest") rather than on the short-term distributional implications of the rules which, in case of general long-term rules, are more uncertain and more difficult to identify. General constitutional rules induce people to accept generally acceptable criteria of equal treatment, due process and fairness. They make it possible to transform the Hobbesian "social

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6 On the distinction between "constitutional choice" and "postconstitutional choice" see J.M. Buchanan, The Limits of Liberty, 1975, pp. 25 ff. The word "constitution" is often used in a formal sense to describe the actual situation of an object, an individual or a community (e.g. the physical constitution of a person). But "constitution" is also used as a normative term, for instance in economic theory in order to denote a set of certain "constitutive principles" and "regulative principles" for the proper functioning of national and international market economies (see above chapter III.4). In legal terminology, the concept "constitution" usually refers to the basic long-term legal rules on which a community is based and by which it is bound. This basic law may be codified in whole or in part in a written "formal constitution". But also in the absence of a written constitution, the basic provisions of a community's legal order are often referred to as a "material constitution". The written "formal constitution" may coincide with the "material constitution" of the legal community concerned. But the formal constitutional document may also include less important or transitional provisions, or it may authorize the legislative body to regulate important "constitutional questions" through the adoption of long-term rules which remain outside the formal constitution but are legally binding upon all members of the community.
able private decisions, constitutional constraints on the governmental taxing, spending, borrowing and regulatory powers are an essential means of inducing governments to pursue policies that are recognized to be in the long-term interest of the community.7

The historical evolution of the old law merchant up to the middle ages (see above chapter II.3) confirms that long-term "constitutional rules" (e.g. on the protection of private contracts and property rights) can be agreed upon also in an "unorganised" international society based essentially on private law. The primary "constitutional function" of these private international commercial rules are to protect individual rights from private intrusions and to coordinate the autonomous individual economic activities so as to make possible mutual gains from international trade. The adoption of national "bills of rights" and written constitutions confirms the contractarian assumption that individuals may be led by their own self-interests to agree on constitutional rules establishing government powers for the performance of specified "protective functions" (e.g. law enforcement and maintenance of peace) as well as certain "productive state functions" (e.g. for the provision of "public goods"). But from the liberal perspective of inalienable human rights as the ultimate source of value and of valuation, the delegated powers are always limited in nature, as explicitly stated in the Ninth Amendment of the US Constitution. The ultimate function of all government activities must consist in protecting and promoting the individual rights and individual welfare of their citizens. At least from a liberal contractarian perspective which seeks to derive and legitimize the constitutional rules of political order from the voluntary agreement of the members of the polity, individuals must be presumed to establish governments for the purpose of protecting and promoting their individual rights.

C) Means of Constitutional Constraint

From the liberal perspective where individuals are the ultimate source of value, the valuation of "private goods" and the determination of "public goods" (e.g. governmental income redistribution) are subjective and cannot be determined as an objective external standard independent of individual preferences. Economic markets and democratic politics are institutional processes enabling per-


powers in the trade policy area. Hence, the need for additional constitutional safeguards.

Most liberal constitutional theories since the 18th century treat the economic and the political system symmetrically as markets in which the outcome is determined by the interaction among individuals pursuing their own and often mutually conflicting self-interests. The same model of the utility-maximizing "homo economicus", applied by the classical economists for their analysis of economic behaviour, is used also for the behaviour of political agents, not because all persons behave in a selfish manner at all times and in all circumstances, but rather because the model reflects inherent tendencies in human behaviour and has proven useful for purposes of "constitutional construction". In order to turn conflict into cooperation and to transform the pursuit of private self-interests into socially beneficial behaviour, there is a need to limit and control the exercise of discretionary government powers through additional constitutional constraints such as:

- rules limiting the domain and admissible instruments of government measures (e.g. limitation of policy powers through the constitutional requirements of "due process" and "proportionality" of policy instruments);
- quantitative and procedural limitations of the government powers to create money, to tax, to borrow, to spend and to redistribute private income (e.g. a "balanced budget requirement" in order to reduce the bias in governmental decision-making towards public debts and budget deficits);
- rules and "accounting procedures" promoting transparent policy-making and competition in the "political market" (e.g. procedural requirements to calculate and publish the costs of alternative policy measures);
- institutional safeguards and separation of government powers so as to reduce the influence of special interests (e.g. transfer of the government power to create money to an independent central bank);
- procedural safeguards strengthening individual rights vis-à-vis both the coercive functions as well as the service functions and redistributive powers of government (e.g. individual access to courts and judicial reviewability of all trade restrictions);
- rules specifying the general constitutional requirements of rule of law, certainty of law, equal treatment, legally limited administrative discretion, fair application of the law (e.g. proportionality and non-retrospective of government interferences into individual rights), protection of acquired rights (e.g. "no expropriation without just compensation"), and of procedural safeguards (e.g. habeas corpus).

9 See J. St. Mill, Considerations on Representative Government, in: Essays on Politics and Society, Collected Works, Vol. 19 (1977), p. 205: "The very principle of constitutional government requires it to be intimated that political power will be abused to promote the particular purposes of the holder, not because it always is so, but because such is the natural tendency of things, to guard against which is the expected use of free institutions". This assumption of utility-maximizing selfish behavior is fully compatible with a step 1 (note 8, p. 79) following remark: "There is such confusion of the ideal that a person ought to be allowed to pursue his own aims with the belief that, if left free, he will or ought to pursue solely his selfish aims. The freedom to pursue one's own aims is, however, as important for the most altruistic person, in whose scale of values the needs of other people occupy a very high place, as for any egoist. It is part of the ordinary nature of men (and perhaps still more of women) and one of the main conditions of their happiness that they make the welfare of other people their chief aim. To do so is part of the normal choice open to us and often the decision generally expected of us. By common opinion our chief concern is this respect should, of course, be the welfare of our family. But we also show our appreciation and approval of others by making them our friends and their aims ours. To choose our associates and generally those whose needs we make our concern is an essential part of freedom and of the moral conception of a free society.

D) How to Provide International "Public Goods" without International Governments? The Need for Internationally Agreed Restraints on National Policy Instruments with Harmful Effects Abroad

Economics distinguishes between privately produced goods and "public goods" that are not produced privately either because consumers cannot be excluded from their use (e.g. in case of a public road) or because their production involves the government monopoly of power. Adam Smith's definition of the three duties of a government 10 limited the list of national public goods to be provided by governments to national defense, law and order, and a limited number of public works and public institutions which it would not pay individuals to produce for themselves. The modern welfare states have considerably extended the list to include, inter alia, stabilization and a "conservative welfare function" (see above chapter V.3.B.c.e). But how can international public goods - such as peace, an open trading system, freedom of communications, monetary stability and le-
gal certainty - which are produced domestically by governments, be produced on the international level without a world government or, at least, without a hegemonic world power interested in supplying international public goods (such as Great Britain during the time of "pax Britannica" and the USA following World War II)?

States are increasingly aware that, in the modern integrated world economy, many national policy objectives and "public goods" can no longer be achieved without voluntary international cooperation and active participation in international organizations as legal and institutional frameworks for the multilateral pursuit of national interests in an interdependent world. Just as voluntary market exchanges of private goods work as a positive-sum game in which the gain for one participant does not imply a loss for another, reciprocal international exchanges of national public goods (e.g. liberalization of national trade barriers, convertibility of the national currency, national treatment of foreign goods and investments) can create international public goods across national frontiers, which a single government could not achieve unilaterally. International guarantees of transnational freedoms and international prohibitions of national government actions with adverse external effects enable a spontaneous, mutually beneficial division of labour among the citizens of different states and can operate as a substitute for "international legislation" by a world government. The contractarian, voluntarily agreed nature of multilateral rules makes it likely that the international rules will be of a general nature allowing individual governments to pursue their separate courses and diverse preferences within the rules. Hence, international "public goods" (such as international legal certainty and open markets) can be produced also without "international governments" through internationally agreed restraints on national policy instruments with harmful effects on other countries.

E) International and Domestic Constitutional Functions of Liberal International Trade Rules

In public international law, the term "constitution" is either used in a formal sense in order to denote multilateral treaties establishing international organizations with legislative and administrative powers of their own. Or it is used in order to denote the substantive, long-term basic rules ("material constitution") of international organizations or of general public international law (e.g. the ba-

Thus, the GATT is sometimes referred to as the "constitution" of the multilateral trading system because the GATT is the only worldwide agreement with general rules of unlimited duration for the liberalization of national trade barriers, the coordination of national trade laws and policies, and the peaceful settlement of international trade disputes. Various GATT rules make it explicitly clear that the basic GATT objective of nondiscriminatory, market-conforming trade competition cannot be achieved unless the basic GATT prohibitions of trade discrimination (e.g. GATT Articles I, II, X) and of non-tariff trade barriers (e.g. GATT Article XI:1) are observed by all GATT contracting parties. GATT Article XXIII, for instance, grants each individual GATT contracting party the right to initiate a multilateral GATT dispute settlement proceeding and to insist on the withdrawal of any GATT-inconsistent discrimination or non-tariff trade barriers by any other GATT contracting party regardless of whether the trade discrimination or non-tariff trade barrier has actually caused trade damage to the complaining country. The GATT rules serve "constitutional functions" on the international level among states by prohibiting harmful trade policy instruments, by limiting (pursuant to Article 41 of the Vienna Convention on the Law of Treaties) the national freedom of contracting parties to conclude "inter-se-agreements" modifying certain multilateral GATT rules as between themselves alone, and by protecting the consistency of the multilateral GATT legal system through collective dispute settlement and enforcement rules. The conception of the basic GATT rules as a "constitution" assists in analysing the inconsistencies between GATT law and GATT practices not only on a case-by-case basis but also as a possible expression of a broader "constitutional failure".

In international state practice and in the literature on public international law, the advantages of liberal international trade rules are often seen only in the rights which the rules grant to governments vis-à-vis other governments (e.g. GATT rights to non-discriminatory access to foreign markets). Also in GATT law are the synallagmatic GATT obligations described as "concessions" (Article

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11 See e.g. A. Verdross, Die Verfassung der Völkerrechtsgemeinschaft, 1926; see also above note 6.