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## The Grey Areas and Yellow Zones of Split Sovereignty Exposed by Globalization: Choosing among Strategies of Avoidance, Cooperation, and Intrusion to Escape an Era of Misguided New Federalism

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THE "GREY AREAS" AND "YELLOW ZONES" OF SPLIT  
SOVEREIGNTY EXPOSED BY GLOBALIZATION:  
CHOOSING AMONG STRATEGIES OF AVOIDANCE,  
COOPERATION, AND INTRUSION TO ESCAPE AN ERA OF  
MISGUIDED "NEW FEDERALISM"

*Matthew Schaefer*\*

I. INTRODUCTION

Numerous commentators claim that globalization is injuring U.S. federalism.<sup>1</sup> However, it is the strategies that governments in the United States are pursuing in response to globalization that are diminishing the values of federalism rather than any aspect of globalization itself.

Globalization is an undeniable phenomenon that encompasses many changes in the world. Two of the most significant changes are increased trade and investment flows between nations<sup>2</sup> and increased non-economic contacts between peoples in different nations. The increased trade and investment is facilitated by international trade and investment agreements as well as improved communications and transportation facilities. Technological advancements in communications and transportation have also lead to the increased non-economic contacts, both direct and indirect, between peoples in different nations. Citizens of one nation have much greater information on the conditions and lives of citizens of other nations today than at any time

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<sup>1</sup> See, e.g., Mark Tushnet, *NAFTA and Federalism in the United States*, 5 CONST. F. 60-62 (Spring/Summer 1994); Barry Friedman, *Valuing Federalism*, 82 MINNESOTA L. REV. 249, 376-77 (1997) (focusing on globalization's manifestation in increased trade and international trade agreements); Candice Hoke, *Arendt, Tushnet, and Lopez: The Philosophical Challenge Behind Ackerman's Theory of Constitutional Moments*, 47 CASE W. RES. L. REV. 903, 914-19 (1997).

<sup>2</sup> With respect to trade, see Renato Ruggiero, *Overview of Developments in International Trade and the Trading System*, WTO FOCUS NEWSLETTER, Jan. 1998, at 3. With respect to investment, see Statement by Under Secretary of State Stuart Eizenstat and Deputy U.S. Trade Representative Jeffrey Lang on the Multilateral Agreement on Investment, *reprinted in* INSIDE U.S. TRADE, Feb. 20, 1998, at 17-19.

previously. This information allows citizens of one nation to care about or otherwise affiliate with citizens of other nations to a greater extent today.

The U.S. federation is often referred to as a split sovereignty.<sup>3</sup> A federation divides power vertically between a central government and sub-federal units. Unlike other forms of decentralized government, federations guarantee some level of autonomy for each level of government.<sup>4</sup> This guarantee is found in a supreme constitution that is not amendable by either level of government and that is umpired by a supreme court.<sup>5</sup> If sovereignty is defined to refer to the holder of supreme power over a given subject matter, then it follows that federations could be referred to as split sovereignties. However, answering questions of constitutional authority are necessary to answer questions of sovereignty. Yet, it is not always clear whether a government maintains constitutional authority to act with respect to a given matter. "Grey areas" in constitutional authority exist. Indeed, grey areas can exist wholly outside the context of sovereignty and extend to whether sub-federal governments have authority to take action in areas in which sovereignty resides in the federal government, but the federal government has not acted. Additionally, even when a government at a particular level maintains sovereignty over a given subject matter, it may face severe political constraints in exercising that sovereignty. The areas in which a government is hesitant to exercise the full extent of its sovereignty as a result of political constraints can be referred to as "yellow zones" (read: proceed with great caution).

Globalization is exposing grey areas and yellow zones in the U.S. split sovereignty to a certain degree. In response to these exposures, governments at both the federal and state level can pursue various strategies. Specifically, in response to exposed grey areas and yellow zones, governments can pursue strategies of avoidance, cooperation, or intrusion. This Article poses the question of whether the strategies pursued by governments in response to this exposure are appropriate in light of the values a federal system of government seeks to promote. In particular, this Article will examine and critique the following strategies: 1) the strategy pursued by the U.S. federal government during the negotiation of international trade and investment agreements seeking further liberalization of trade and investment policies maintained by sub-federal governments; and 2) the strategy pursued by state governments in

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<sup>3</sup> See, e.g., *U.S. Term Limits v. Thornton*, 115 S.Ct. 1842, 1972 (1995) (Kennedy, J. concurring) ("The Framers split the atom of sovereignty").

<sup>4</sup> See DANIEL ELAZAR, *EXPLORING FEDERALISM* 23 (1987); Martin Redish, *Constitutionalizing Federalism: A Foundational Analysis*, 23 OHIO N. U.L. REV. 1237, 1240 (1997).

<sup>5</sup> See TASK FORCE ON CANADIAN UNITY, *COMING TO TERMS: THE WORDS OF THE DEBATE*, at 4 (Feb. 1979). See also STEPHAN KUX, *SOVIET FEDERALISM: A COMPARATIVE PERSPECTIVE* 7 (Inst. for East-West Security Studies, 1990).

engaging in foreign affairs in an era of increased trade, information, communication, transportation, and corresponding affiliation between peoples in various nations.

The analysis and critique of the U.S. federal and state government strategies reveal that the United States is in danger of adopting a misguided notion of "new federalism." The strategies pursued by the governments in the United States preserve and promote the autonomy of states in a manner that allows for policies creating negative externalities, beggar-thy-neighbor policies, and other sub-optimal policies arising out of prisoner's dilemma-type situations. Moreover, the strategies preserve state autonomy in a manner that does not lead to greater public participation in democracy or useful experimentation. In short, the strategies chosen by the governments in the United States do not promote the values of federalism. A brief comparative examination of strategies pursued by the Canadian governments supports this conclusion. Indeed, the comparison yields what will likely be surprising results to many observers. The U.S. federal government has arguably been less aggressive in constraining sub-federal government protectionism vis á vis Canada and U.S. states are arguably more aggressive than their provincial counterparts in establishing foreign policies.<sup>6</sup> Accordingly, the governments in the United States must undertake a re-examination of their current strategies. Such a re-examination should occur in the context of implementing a model for a "new federalism" that focuses on the values a federal system of government seeks to promote rather than allowing federalism to be a mere slogan or rhetorical device. Successful implementation of such a model will require conscientious politicians that not only assess the constitutionality of their actions<sup>7</sup> but, in addition, assess the impact of their actions on the values of federalism.

Part II of this Article discusses the lack of serious consideration of the values of federalism in the current politics of "new federalism." It argues that conscientious politicians should weigh the values of federalism before taking action with respect to a given matter. Part III defines grey areas and yellow zones in the context of split sovereignty and explores their relationship. Part IV identifies the grey areas and yellow zones present in U.S. federalism. Part V analyzes the various strategies that can be adopted by federal and state governments in response to grey areas and yellow zones exposed by global-

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<sup>6</sup> I am not arguing that the Canadian government has achieved greater liberalization at the sub-federal level than the U.S. government. Rather, the strategy pursued by the Canadian federal government is arguably more aggressive in light of the significant grey areas that government faces in negotiating and implementing trade agreements.

<sup>7</sup> See Paul Brest, *The Conscientious Legislator's Guide to Constitutional Interpretation*, 27 STANFORD L. REV. 585 (1974).

ization. Part VI critiques the actual strategy adopted by the U.S. federal government with respect to the negotiation of international trade agreements. Part VII critiques the strategy chosen by state governments with respect to engaging in foreign affairs. Part VIII briefly compares the strategies of governments in Canada to highlight the misguided "new federalism" apparent in the strategies of U.S. governments. Part IX concludes that the U.S. federal and state governments need to modify their strategies adopted in response to globalization in the context of an overall reassessment of "new federalism."

## II. "NEW FEDERALISM" RENEWED: RHETORIC, VALUES, AND THE CONSCIENTIOUS POLITICIAN

Since the adoption of the wide federal programs under the "New Deal" engineered by President Franklin Delano Roosevelt in the 1930s, various U.S. presidents have proposed returning power to the states.<sup>8</sup> Most prominent was President Ronald Reagan's call for a "new federalism" that would devolve power to the states.<sup>9</sup> Demands for devolution of certain powers to the states have returned with great force within the past few years.<sup>10</sup>

Despite this renewed call for a "new federalism," there is little careful consideration by politicians of whether the values of federalism are promoted by federal or state action with respect to a given matter.<sup>11</sup> As a result, "new federalism" risks devolving authority to the states or preserving state autonomy in instances in which the values of federalism are not promoted. The U.S. Constitution does not explicitly require politicians at various levels of government to weigh the values of federalism when deciding whether to act on a given issue. However, the failure of politicians to do so conscientiously is leading to a diminution in the benefits that a federal system was intended to bring to those governed. While one frequently hears of federalism in political debates, politicians often use federalism as a rhetorical tool to argue for their underlying policy objectives (or perhaps the objectives of special interest groups) rather than in the context of a debate over whether the values of federalism will be promoted by a particular action.<sup>12</sup>

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<sup>8</sup> See John Kincaid, *The New Federalism Context of the New Judicial Federalism*, 26 RUTGERS L.J. 913 (1995).

<sup>9</sup> See *id.*; Rena Steinzor, *Unfunded Environmental Mandates and the "New (New) Federalism": Devolution, Revolution, or Reform*, 81 MINN. L. REV. 97, 124-30 (1996).

<sup>10</sup> See Mark Tushnet, *Living in a Constitutional Moment? Lopez as Constitutional Theory*, 46 CASE W. RES. L. REV. 845, 848-50 (1996) (discussing the Contract with America and related demands for a devolution of power to state governments).

<sup>11</sup> Friedman, *Valuing Federalism*, *supra* note 1.

<sup>12</sup> Norman Redlich & David Lurie, *Federalism: A Surrogate for What Really Matters*, 23 OHIO N. U. L. REV. 1273 (1997).

Political scientists,<sup>13</sup> political economists, institutional economists,<sup>14</sup> and the Constitution's Founders<sup>15</sup> have enumerated the primary considerations that must be weighed in achieving the appropriate balance between federal regulation and state autonomy in a federal system of government. The benefits of state autonomy in a federal system include greater public participation in democracy,<sup>16</sup> providing laboratories for experimentation,<sup>17</sup> and allowing maximization of different preference sets of various territorial populations.<sup>18</sup> The benefits of constraining state autonomy and promoting federal action include avoiding policies leading to negative externalities,<sup>19</sup> beggar-thy-neighbor policies,<sup>20</sup> and other sub-optimal policies arising out of prisoner's dilemma-type situations.<sup>21</sup> In deciding whether federal regulation or state autonomy is appropriate with respect to a given issue, politicians must conscientiously consider and weigh the values of federalism. Since conscientious politicians at the federal and state level may disagree after weighing the values of federalism, an overall reassessment will need to occur. Politicians are less likely to conduct self-interested weighing with respect to particular matters if they know that numerous areas of regulation will be reassessed simultaneously or in close succession since an honest reassessment will likely point to devolution of power to the states in some areas and elevation of power to the federal government in other areas. In other words, "trade-offs" in matters regulated by federal and state governments can occur in an overall reassessment to promote the values of federalism. Without the possibility of trade-offs, politicians (even conscientious ones) may be tempted to conduct a

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<sup>13</sup> See, e.g., ELAZAR, *EXPLORING FEDERALISM*, *supra* note 4, at 84-103 (1987).

<sup>14</sup> Joel Trachtman's writings apply institutional economic theory to questions of the vertical and horizontal division of authority in governments. See, e.g., Joel Trachtman, *Reflections on the Nature of the State: Sovereignty, Power, and Responsibility*, 20 *CAN.-U.S. L.J.* 399 (1994) [hereinafter Trachtman I]; Joel Trachtman, *International Regulatory Competition, Externalization, and Jurisdiction*, 34 *HARV. INT'L L.J.* 47 (1993) [hereinafter Trachtman II].

<sup>15</sup> See Michael McConnell, *Federalism: Evaluating The Founders' Design*, 54 *U. CHI. L. REV.* 1484, 1493-1500 (1987).

<sup>16</sup> See, e.g., Friedman, *supra* note 1, at 389-90.

<sup>17</sup> See, e.g., *id.*, at 397-98.

<sup>18</sup> See Trachtman I, *supra* note 14, at 413; Trachtman II, *supra* note 14, at 100-03.

<sup>19</sup> See Friedman, *supra* note 1, at 407.

<sup>20</sup> A beggar-thy-neighbor policy is a policy instituted by a large economic jurisdiction that, in the short-term, benefits the jurisdiction at the expense of other jurisdictions. However, since other large jurisdictions respond in kind, such policies ultimately reduce the welfare of both jurisdictions. The optimal tariff argument is an example of a beggar-thy-neighbor policy.

<sup>21</sup> See, e.g., Matthew Schaefer, *State Investment Attraction Subsidy Wars Resulting From a Prisoner's Dilemma: The Inadequacy of State Constitutional Solutions and the Appropriateness of a Federal Legislative Response*, 28 *N. M. L. REV.* 303 (1998).

self-interested weighing of the values of federalism in order to protect their governmental power.<sup>22</sup>

Why must the politicians engage in a weighing of the values of federalism? Is it not the role of courts to preserve the appropriate federal balance? Certainly, courts have a role to play and they could engage in careful weighing of the values of federalism. However, in practice, the courts have shown little inclination to engage in a weighing of the values of federalism.<sup>23</sup> Moreover, courts cannot be the sole guardians of the values of federalism because courts face various constraints that the political branches do not. First, courts appear constrained by doctrinal limits. For instance, courts have struck down protectionist state regulations and taxes under the dormant Commerce Clause, but have been unwilling to strike down equally protectionist purchasing and subsidies practices in part because of the history and language of the Commerce Clause. Second, courts are unable to force the political branches to affirmatively use their powers when use of such powers would promote the values of federalism. Courts are simply able to protect the values of federalism in some instances from injurious incursions by the federal government and state governments. Third, courts are constrained by *stare decisis*. Indeed, *stare decisis* may prevent courts from adjusting the federal balance to changed conditions, or increased knowledge of conditions, that affect the weighing of the values of federalism.<sup>24</sup> Lastly, courts are limited to addressing "cases and controversies" appropriately placed before them and thus they cannot necessarily reassess numerous regulatory areas at once.

Are there any other possible policemen to ensure that the values of federalism are fully promoted? One might look toward businesses affected by federal and state regulation. However, businesses lack the proper incentives to persuade courts and legislatures to undertake a meaningful weighing of the values of federalism. Businesses bring cases and lobby based on profit motives, not on the basis of promoting the values of federalism. The profit motives of businesses may align with the promotion of the values of federalism in many instances, but certainly not in all instances. Thus, the overall reassessment that is required can only occur with conscientious politicians implementing a "required consideration" model of federalism in which politi-

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<sup>22</sup> See, e.g., Trachtman II, *supra* note 14, at 99 (noting in the context of vertical allocation of powers within the European Community that a "horse trading approach" may be necessary).

<sup>23</sup> See Erwin Chemerinsky, *The Values of Federalism*, 47 FLA. L. REV. 494, 501-02, 524-25 (1995); Friedman, *supra* note 1, at 318-19.

<sup>24</sup> See Larry Kramer, *Understanding Federalism*, 47 VANDERBILT L. REV. 1488, 1499-1500 (1994).

cians are required to carefully weigh the values of federalism before acting on a given issue.<sup>25</sup>

As in all matters, the conscientious politician should weigh the values of federalism when choosing among strategies of avoidance, cooperation, and intrusion in response to grey areas and yellow zones exposed by globalization. However, in practice there is very little consideration of the values of federalism when formulating these strategies. Before examining the risks and rewards of various strategies with regard to the values of federalism, it is necessary to further analyze grey areas and yellow zones in the context of split sovereignty and to identify the current grey areas and yellow zones of U.S. federalism.

### III. GREY AREAS AND YELLOW ZONES: DEFINED, RELATED, AND DISTINGUISHED IN THE CONTEXT OF SOVEREIGNTY, AUTHORITY, AND THE EXERCISE OF AUTHORITY

Sovereignty can be defined as the holder of supreme power over a given matter.<sup>26</sup> In federations, such as the United States, sovereignty so defined is divided between the federal government and state governments. However, the sovereignty, or supreme power, of the federal government is not in question in those matters in which it has constitutional authority to act. The Supremacy Clause of the constitution makes federal law supreme to state law.<sup>27</sup> Thus, the question of whether the federal government maintains constitutional authority to act with respect to a given matter must be answered in order to determine which level of government maintains sovereignty over a given matter. If the federal government has constitutional authority to act, then it has supreme power over the matter. If the federal government does not have constitutional authority to act, then state governments are sovereign with respect to the matter and indeed enjoy exclusive jurisdiction over the matter. However, questions of authority can arise outside the context of sovereignty. In certain areas where the federal government has authority to act (and thus has sovereignty) but has failed to do so, it must be determined whether states have authority to act until the federal government exercises its supreme power. If it is determined that states have authority to act in such a

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<sup>25</sup> I borrow the idea (and the term) "required consideration" model from Martin H. Redish, *Constitutionalizing Federalism: A Foundational Analysis*, 23 OHIO N. U. L. REV. 1237 (1997).

<sup>26</sup> See, e.g., Matthew Schaefer, *National Review of WTO Dispute Settlement Panel Reports: In the Name of Sovereignty or Enhanced WTO Rule Compliance?*, 11 ST. JOHN'S J. LEGAL COMMENT. 307, 329-33 (1996) (discussing various definitions of sovereignty in the context of international trade agreements).

<sup>27</sup> U.S. CONST., art. VI.



situation, then concurrent jurisdiction of the federal and state governments exists. If states have no authority to act in such an instance, then the federal government enjoys exclusive jurisdiction over the matter.

Thus, questions of authority are important to determine sovereignty and to determine areas of exclusive and concurrent jurisdiction. However, the constitutional authority of a government to take action with respect to a given matter can be unclear. These areas can be referred to as "grey areas." Grey areas can be "one way" phenomenon such that action by one level of government in an area is clearly allowed, but legal authority for action by the other level of government is uncertain.

Maintaining constitutional authority to act does not necessarily mean a government is politically able to act. Yellow zones represent those areas in which a government has clear legal authority to act, but faces political limitations in exercising such authority. As with grey areas, yellow zones can be "one way" phenomenon that affect only one level of government. Grey areas can be considered a sub-set of all yellow zones since action within a grey area is likely to be politically difficult in addition to having uncertain legal authority.

Yet, it is important to further distinguish grey areas and yellow zones in order to understand the complex interaction that can exist between the two. Changed politics alone can eliminate a yellow zone. In contrast, grey areas of split sovereignty can frequently be resolved by the courts alone. However, in some instances, the situation is somewhat more complex than this distinction between grey areas and yellow zones. Sometimes federal government action can resolve a grey area. This can occur in an area in which the federal government has clear authority to act, state government authority to act is unclear, and federal action with respect to the matter will preempt the state action as a result of the Supremacy Clause. But, preemptive federal action with respect to the matter may fall within a yellow zone. In such instances, eliminating the yellow zone inhibiting federal action can also eliminate the grey area that exists with respect to state action. In such instances, the grey area is resolved without the aid of the courts.

#### IV. IDENTIFICATION OF GREY AREAS AND YELLOW ZONES IN U.S. FEDERALISM

##### A. Grey Areas of Authority with Regard to External Affairs

The U.S. Supreme Court has often described the power of the U.S. federal government over foreign affairs as "exclusive,"<sup>28</sup> despite the fact that the Constitution does not grant a general foreign affairs power. Indeed, the U.S. Constitution does not mention the term "foreign affairs."<sup>29</sup> Instead, the Constitution grants branches of the federal government certain powers related to foreign affairs while denying other such powers to the states. The Constitution grants the President the power to enter into treaties and the power to appoint ambassadors with varying levels of advice and consent of the Senate,<sup>30</sup> and declares the President to be commander-in chief of the armed forces.<sup>31</sup> The Constitution grants Congress the power to regulate foreign commerce, declare war, and define and punish crimes against the law of nations.<sup>32</sup> Correspondingly, the Constitution prohibits the states from entering into treaties.<sup>33</sup> It further prohibits states, without the consent of Congress, from laying duties on imports or exports, keeping troops, or entering into any agreement or compact with a foreign power.<sup>34</sup> Grey areas with respect to foreign affairs powers arise out of difficulties in interpreting the explicit grants and denials of authority as well as the failure of the constitution to grant a general foreign affairs power. The analysis below looks first at the grey areas involved in the interpretation of a few explicit clauses and then at the more general grey area implicating state foreign affairs legislation.

##### 1. Interpreting the Compacts and Agreement Clause

Practice, court decisions, and Congressional documents indicate that not all agreements and compacts are covered by the constitutional clause that prohibits states from entering into agreements or compacts with foreign pow-

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<sup>28</sup> U.S. v. Pink, 315 U.S. 203, 233 (1942). *See also* U.S. v. Belmont, 301 U.S. 324 (1937); U.S. v. Curtiss-Wright Export Corp., 299 U.S. 304, 317 (1936).

<sup>29</sup> *Contrast* the U.S. Constitution's failure to grant a general foreign affairs power *with* the Australian Constitution that grants the Parliament the power to legislate with respect to "foreign affairs." *See* AUSTR. CONST., § 51(29).

<sup>30</sup> U.S. CONST., art. II, § 2 (entering into treaties requires the consent of two-thirds of the Senate; appointing Ambassadors requires the consent of a simple majority of Senators).

<sup>31</sup> *See id.*

<sup>32</sup> *See id.*, art. I, § 8.

<sup>33</sup> *See id.*, art. I, § 10.

<sup>34</sup> *See id.*

ers without the consent of Congress.<sup>35</sup> The Supreme Court stated earlier in this century that Congressional assent is not required for all compacts or agreements entered into by the states, only those that tend to "increase the powers of the states or to encroach upon the just supremacy of the United States."<sup>36</sup> This contrasts with the view taken by at least four justices on the Supreme Court in the mid-1800s that all agreements whether written or oral would require Congressional consent.<sup>37</sup> During this century, the federal government has also apparently relaxed its interpretation of the new standard.<sup>38</sup> Indeed, hundreds of agreements exist between U.S. states and Canadian provinces that have not received Congressional approval.<sup>39</sup> But what exactly does the standard "increase the power of the states or encroach upon the just supremacy of the United States"<sup>40</sup> encompass? It seems clear that an agreement between a state and a foreign government (or sub-federal government in a foreign country) that was intended to be binding under international law would require Congressional consent under this standard.<sup>41</sup> However, an examination of agreements receiving Congressional approval indicate that the standard must capture additional types of agreements. Indeed, most agreements receiving Congressional approval deal with relatively mundane topics, including the construction of a highway bridge, establishment of an authority to operate a highway bridge, and cooperation on forest fires.<sup>42</sup> Nonetheless, one agreement, the Great Lakes Basin Compact, did raise significant issues.<sup>43</sup> Congressional approval of the compact did not extend to original provisions

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<sup>35</sup> See S. Doc. 232, 74th Cong., 2d Sess. at 366, 368; *McHenry County v. Brady*, 163 N.W. 540 (N.D. 1917); LOUIS HENKIN, *FOREIGN AFFAIRS AND THE UNITED STATES CONSTITUTION* 151-156 (Oxford Univ. Press, 2d ed., 1996); Raymond S. Rodgers, *The Capacity of States of the Union to Conclude International Agreements: The Background and Some Recent Developments*, 61 AM. J. INT'L L. 1021 (1967).

<sup>36</sup> *McHenry County*, *supra* note 35, at 541.

<sup>37</sup> *Holmes v. Jennison*, 39 U.S. 540, 572-74 (1840).

<sup>38</sup> For example, in the late 1930s, the State Department declared, in response to a question by the California Department of Motor Vehicles, that an arrangement for reciprocal exemption of registration and fees with the Mexican territory of Baja would require Congressional consent. See Hackworth, 5 DIG. OF INT'L L. & PRAC. 24, sec. 464. It is doubtful the federal government would hold a similar view with respect to such an agreement today. See also John Kincaid, *Constituent Diplomacy: U.S. State Roles in Foreign Affairs*, in CONSTITUTIONAL DESIGN AND POWER SHARING IN THE POST-MODERN EPOCH 107, 118-19 (Daniel Elazar ed. (1991)).

<sup>39</sup> See LUIGI DI MARZO, *COMPONENT UNITS OF FEDERAL STATES AND INTERNATIONAL AGREEMENTS* 82-84 (Sijthoff & Noordhoff, 1980); Kincaid, *supra* note 38, at 131-32.

<sup>40</sup> *McHenry County*, *supra* note 35, at 541.

<sup>41</sup> Although he does not explicitly so state, I find Professor Henkin's views in accord with this statement. See Henkin, *supra* note 35, at 155.

<sup>42</sup> See *id.* at 153.

<sup>43</sup> Great Lakes Basin Compact, Pub. L. No. 90-419 (1968).

of the compact that would have given the commission established by the compact the power to recommend treaties between federal governments and cooperate with foreign governments or subdivisions on environmental and other matters.<sup>44</sup> The scant court opinions and the practice of governments in applying the standard leaves the area shaded in grey.

The wording of the agreements and compacts clause also opens another grey area: to what extent can states engage in negotiations with foreign powers? Some commentators have argued that states can engage in negotiations with a foreign power since there are no explicit limits in the Constitution on negotiations between a state and a foreign power.<sup>45</sup> Since states can enter into agreements, these commentators presume that states can negotiate an agreement prior to receiving Congressional approval. But can it be plausibly argued that a state could begin negotiating with a foreign government on any topic, for example, negotiate with India and Pakistan on the banning of nuclear tests? Of course, existing federal statutes may prohibit state officials from engaging in such conduct,<sup>46</sup> but it may be that such limits would exist from the very structure of the Constitution. Nonetheless, states have entered into numerous agreements with the Canadian provinces prior to or without Congressional approval, and thus, ipso facto they have entered into negotiations with Canadian provinces without receiving Congressional approval. Regional governors' associations, such as the Western Governors Association and the Border State Governors, also have discussions with their Canadian provincial and Mexican state counterparts at meetings and conferences. As with agreements themselves, the lack of court opinions and the practice of governments leaves the area of negotiations shrouded in some grey.

## 2. Power of the President to Appoint Ambassadors

Another grey area arising out of a specific clause relates to the power granted to the President to appoint ambassadors. In spite of this clause, nearly all states have established overseas trade and investment offices and state governors routinely lead trade missions to foreign countries accompanied by in-state business interests.<sup>47</sup> However, most of the investment offices

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<sup>44</sup> *Id.*, sec. 2.

<sup>45</sup> Michael Shuman, *Dateline Mainstreet: Courts v. Local Foreign Policies*, 86 FOREIGN POL'Y 158, 163 (1992).

<sup>46</sup> Logan Act, 18 U.S.C. § 953 (prohibiting any citizen, including presumably a state official, without authority of the United States from carrying on "correspondence or intercourse with any foreign government . . . with intent to influence the measures or conduct of any foreign government . . . in relation to any disputes or controversies with the United States, or defeat the measures of the United States").

<sup>47</sup> NATIONAL GOVERNORS' ASS'N, *GOING GLOBAL: A GOVERNOR'S GUIDE TO INTERNATIONAL TRADE* (1992).

and trade missions can be considered "in-person advertising" that primarily focus on information exchange and establishing business contacts. Such offices and missions generally do not focus on seeking a change in the investment, trade, or other public policies of foreign governments. As such it is unlikely that such activities interfere with the President's powers to appoint Ambassadors. However, no court case has dealt with the federalism dimensions of this clause.

### 3. Dormant Foreign Affairs Doctrine

A wider-band grey area exists outside the interpretation of specific clauses of the Constitution explored above. While there is no dispute that the federal government's powers over foreign affairs are plenary and supreme, a dispute exists as to whether and to what extent such powers are exclusive with respect to matters that the states are not explicitly prohibited by the Constitution from undertaking. In other words, there is controversy over whether and to what extent there is what might be called a "dormant foreign affairs doctrine" that prevents the states, even in the absence of federal government action preempting the states, from enacting legislation with either a foreign policy motive or a direct effect on U.S. foreign relations.<sup>48</sup> Specifically, there is a question whether the default rule should be that states have authority to legislate with respect to foreign affairs until the federal government acts to preempt such legislation or that states cannot act in such instances even in the absence of an affirmative federal pronouncement (e.g., where the federal government is utilizing quiet diplomacy or pressure in international organizations). Additionally, questions arise depending on the default rule established. If the default rule is that states maintain authority to act until the federal government acts, the question arises as to whether the federal act must explicitly preempt the state activity or the existence of a federal act itself should by implication preempt state activity. If the default rule is that states cannot act even in the absence of a federal pronouncement, the question arises whether only state regulation should be covered by such a default rule or market participant activity of a state (i.e., procurement and subsidies) should also be covered.

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<sup>48</sup> See *Zschemig v. Miller*, 389 U.S. 429 (1969) (adopting, or seeming to adopt, an effects test for such a doctrine, but containing language that would support motive review as well). See also Richard Bilder, *The Role of States and Cities in Foreign Relations*, 83 AM. J. INT'L L. 821, 825-26 (1989) (noting that "scholars and judges have continued to puzzle over [Zschemig's] reasoning and scope, and, in particular, over precisely where and how the courts should draw the line between constitutionally permissible and prohibited state and local action"). Henkin, *supra* note 35, at 165 ("One would be bold to predict that [Zschemig] has a future life . . ."). The existence of such a doctrine has recently been criticized. See Jack Goldsmith, *Federal Courts, Foreign Affairs, and Federalism*, 83 VA. L. REV. 1617 (1997).

In the 1968 *Zschernig* case,<sup>49</sup> the Supreme Court appeared to formulate a default rule that states could not act in a manner that unduly interfered with foreign affairs even in the absence of preemptive federal legislation. Several lower courts have relied on the doctrine in striking down state statutes, but the Supreme Court has never revisited the doctrine.<sup>50</sup> The doctrine has come under increasing criticism and, in any event, is surrounded by considerable uncertainty.<sup>51</sup>

## B. Grey Areas of Authority With Regard to Internal Affairs

The U.S. Constitution grants certain enumerated powers to federal government. The 10th Amendment of the Constitution, in turn, reserves all power to the states and the people that is not delegated to the federal government. The most significant or expansive power granted to the federal government is the power to regulate interstate and foreign commerce.<sup>52</sup> Since the 1930s the Supreme Court has recognized that the federal government can regulate matters with a significant effect on interstate and foreign commerce.<sup>53</sup> However, at various times over the past several decades the Supreme Court has sought to impose outer limits on the use of the commerce power. In establishing these outer limits, the Court has often referred to the 10th Amendment and, on other occasions, to the federal structure of government created by the Constitution. The first such attempt occurred in the mid-1970s.<sup>54</sup> The Court held in *National League of Cities* that the federal government could not act against the states in a manner "that would impair the states' ability to function effectively in the federal system."<sup>55</sup> Specifically, the federal government could not interfere with the integral government functions of state bodies providing traditional government services.<sup>56</sup> However, the Court abandoned the *National League of Cities* doctrine in the mid-1980s due to frustration over applying its standard. The Court held in *Garcia* that the political process itself provided sufficient protection of state auton-

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<sup>49</sup> See *Zschernig*, *supra* note 48.

<sup>50</sup> See, e.g., *Bethlehem Steel Corp. v. Board of Comm. of L.A. Dept. of Water & Power*, 276 Cal. App.2d 227 (Cal. App. 1969); *Springfield Rare Coin Galleries v. Johnson*, 503 N.E.2d 300 (Ill. 1986).

<sup>51</sup> See *Bilder*, *supra* note 48 (questioning the scope of the doctrine); *Goldsmith*, *supra* note 48 (criticizing the doctrine).

<sup>52</sup> U.S. CONST., art. I, § 8, cl. 3.

<sup>53</sup> See, e.g., *Wickard v. Filburn*, 317 U.S. 111 (1942).

<sup>54</sup> *National League of Cities v. Usery*, 426 U.S. 833 (1976), *overruled by Garcia v. San Antonio Metropolitan Transit Authority*, 469 U.S. 528 (1985).

<sup>55</sup> *National League of Cities*, 426 U.S. at 852 (citing *Fry*, 421 U.S. at 547, n.7).

<sup>56</sup> *Id.* at 851.

omy within the Constitution.<sup>57</sup> This decade the Court has once again sought to establish judicially imposed outer limits on Congress' commerce power. In *New York v. United States* and *Printz*, the Court stated that Congress could not commandeer state legislatures to enact, or state executive official to enforce, federal regulatory programs.<sup>58</sup> In *Lopez*, the Court sought to rein in use of the commerce power to regulate activities not of a commercial nature and only having an impact on interstate commerce through an attenuated chain of events.<sup>59</sup> The doctrines established by these cases, *Lopez* in particular, await further definition. In the interim, Congress faces a narrow-band of grey regarding use of its commerce power.

In terms of implementing international agreements, the Supreme Court ruled in *Missouri v. Holland* earlier in this century that the federal government could pass legislation to implement a treaty even if it did not have the power to pass the legislation in the absence of the treaty.<sup>60</sup> Senator Bricker of Ohio led a movement in the early 1950s to amend the Constitution so as to change this rule of *Missouri v. Holland*.<sup>61</sup> However, his effort failed. Thus, judicially imposed outer limits may not apply to legislation implementing a treaty. However, treaties requiring two-thirds approval by the Senate are not the only constitutional method for the United States to enter into an international agreement.<sup>62</sup> Some international agreements are approved by a simple majority of both houses of Congress relying on Congressional power to regulate foreign trade and to make all laws necessary and proper for executing that power.<sup>63</sup> In contrast to treaties, it is likely that judicially imposed outer limits would apply to Congressional-Executive agreements.<sup>64</sup>

Other narrow limits on federal government's power to implement treaties or enact federal legislation exist and some of these limits possess a grey hue.

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<sup>57</sup> *Garcia*, 469 U.S. 528 (1985).

<sup>58</sup> *New York v. U.S.*, 505 U.S. 144 (1992); *Printz v. U.S.*, 117 S.Ct. 2365 (1997).

<sup>59</sup> *U.S. v. Lopez*, 514 U.S. 549 (1995).

<sup>60</sup> 252 U.S. 416 (1920)

<sup>61</sup> See John Whitton & Edward Fowler, *Bricker Amendment-Fallacies and Dangers*, 48 AM. J. INT'L L. 23 (1954); Thomas Burgenthal, *The U.S. and International Human Rights*, 9 HUM. RIGHTS L.J. 141, 145-47 (1988). Under section 2 of the Bricker Amendment, a treaty would become "effective as internal law of the U.S. only through legislation that would be valid in the absence of a treaty." Sen. Rep. 412 accompanying S.J.Res. 1, 83rd Cong., 1st Sess. (1953).

<sup>62</sup> RESTATEMENT (THIRD) OF FOREIGN RELATIONS LAW OF THE UNITED STATES, § 303(2) (1987); John Jackson, *United States, in THE EFFECT OF TREATIES IN DOMESTIC LAW* (Francis Jacobs & Shelly Roberts eds. (1987)).

<sup>63</sup> See *id.* See also Bruce Ackerman & David Golove, *Is NAFTA Constitutional?*, 108 HARV. L. REV. 799 (1995).

<sup>64</sup> See Matthew Schaefer, *The 21<sup>st</sup> Century Trade Negotiator's Guide to Late 20<sup>th</sup> Century U.S. Supreme Court Federalism Jurisprudence* (article on file with author).

For instance, the 21<sup>st</sup> Amendment provides that "the transportation or importation into any State . . . for delivery or use therein of intoxicating liquors, in violation of the laws thereof, is hereby prohibited." The purpose behind this amendment was to allow states to regulate the "time, manner and place" of the delivery and sale of alcoholic beverages, but not to protect the local alcoholic beverage industry. Accordingly, the limits the 21<sup>st</sup> Amendment places on the federal government's power are quite narrow.<sup>65</sup> However, since Supreme Court jurisprudence under the 21<sup>st</sup> Amendment has focused on tax matters, there is at least some grey over the exact extent of federal authority with respect to non-tax matters such as distribution.

### C. Yellow Zones in the Exercise of Authority

The yellow zones in the U.S. federation are more easily analyzed. One might go so far as to claim in the current political climate that any federal action that limits existing levels of state autonomy falls within a yellow zone. Proposals for a "Conference of the States" focusing on a return of power to the states and certain proposals in the Republican Congress' "Contract With America" are indications that federal action that constrains existing state autonomy is becoming increasingly difficult politically. If one finds this claim somewhat exaggerated, and one could likely find recent examples to the contrary, it is undoubtedly the case that the federal government faces a yellow zone in terms of limiting state autonomy through international agreements<sup>66</sup> and limiting state fiscal policies, such as taxation, procurement, and subsidies.

## V. STRATEGIES OF AVOIDANCE, COOPERATION, AND INTRUSION: RISKS AND REWARDS IN TERMS OF THE VALUES OF FEDERALISM

When an element of globalization exposes a grey area or yellow zone in the split sovereignty of a federation, governments can respond with three general strategies: avoidance, cooperation, or intrusion. Each strategy pur-

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<sup>65</sup> *Capital Cities Cable v. Crisp*, 467 U.S. 691, 716 (1984); *Bacchus Imports v. Dias*, 468 U.S. 263, 276 (1984).

<sup>66</sup> This Article focuses on international trade agreements. For a discussion of federal hesitancy in constraining states through international human rights agreements and possible solutions to overcoming the problem, see Peter Spiro, *The States and International Human Rights*, 66 *FORDHAM L. REV.* 567 (1997). I should note that the values of federalism carry different weights in the context of binding state governments to certain international human rights norms as compared with international trade agreements obligations. The benefits of state autonomy, including public participation in democracy, serving as laboratories of experimentation, and maximizing preference sets of non-economic values of different territorial populations, are potentially threatened more by certain international human rights norms (e.g., those prohibiting the death penalty) than international trade agreements.



sued comes with certain risks and rewards for the values of federalism (and indeed the survival of federalism). The risks and rewards can differ depending on whether a grey area or yellow zone is implicated. These risks and rewards are best identified in specific contexts. Accordingly, the risks and rewards in the context of federal government negotiation of international trade and investment agreements seeking liberalization of sub-federal government policies and sub-federal government engagement in foreign policy are examined separately below.

#### A. Federal Government Negotiation of International Trade and Investment Agreements

If a federal government pursues a strategy of avoidance in international trade negotiations, then the autonomy of the sub-federal governments will be preserved. But autonomy to do what? International trade and investment agreements prohibit measures that discriminate against foreign goods, services, and investments. Thus, an avoidance strategy allows protectionist, beggar-thy-neighbor regulation to persist. There is no need to allow states to experiment with discriminatory laws since experimentation in the form of protectionism has been tried and has been proven a failure. Such autonomy generally does not increase public participation in a democracy since, if public choice theory has any descriptive force, protectionist laws generally tend to result from successful lobbying by concentrated special interests. If international trade and investment agreements mandated harmonization, then beneficial aspects of state autonomy would be implicated. Sub-federal governments would not be free to experiment with different tax rates or levels of consumer safety. Sub-federal governments would not be able to maximize the preference sets of their territorial populations with respect to various quality-of-life issues. However, international trade and investment agreements currently do not mandate harmonization of tax policies or standards relating to quality-of-life issues.

A strategy of intrusion by a federal government into yellow zones and possibly grey areas that are filled with sub-federal government protectionist policy has the benefit of seeking the elimination of sub-federal autonomy exercised for protectionist purposes. Sub-federal autonomy is reduced, but only in a manner that promotes the values of federalism. Action by federal authorities is appropriate to overcome beggar-thy-neighbor policies. However, a strategy of intrusion carries the cost of increased intergovernmental friction. Intergovernmental frictions may be an important consideration because, in the extreme, such frictions can lead to dissolution of the federation. Even milder frictions in stable federations with respect to a particular issue can spoil cooperation between federal and sub-federal governments on other

important issues. Moreover, in the case of intrusion into a grey area, a federal government risks possible clarification of the grey area in favor of sub-federal governments by the courts. Courts, as noted before, may not rely on a careful weighing of the values of federalism when making determinations and clarifying grey areas. The less significant the intrusion, the less likely a legal challenge leading to clarification will occur. To the extent a grey area is implicated, the shade of grey will also influence the likelihood of a legal challenge leading to clarification.

A strategy of cooperation involves a federal government discussing with sub-federal governments the benefits of reducing sub-federal autonomy to enact measures that discriminate against foreign goods, services, and investments and seeking some form of consent from sub-federal governments for liberalization. A strategy of cooperation between federal and sub-federal governments could lead to the elimination of beggar-thy-neighbor policies in a manner that does not cause (significant) friction. To the extent a grey area is implicated, cooperation also lessens the chances of challenge in the courts. In addition to minimizing intergovernmental frictions and the possibility of legal challenges resulting from a unilateral intrusion into a grey area or yellow zone, a strategy of cooperation can lead to a significant reduction in sub-federal autonomy used for protectionist purposes. Indeed, a successful strategy of cooperation may turn a yellow zone into a "green zone." (Read: proceed with course of action). However, the bargaining that occurs in the context of a cooperation strategy is influenced by the perceived strategy that will be followed should cooperation fail. Thus, it is important for a federal government to be aware of perceptions maintained by sub-federal governments regarding the "fallback" strategy of the federal government.

## B. State Government Engagement in Foreign Policy

A strategy of intrusion by a sub-federal government with respect to the grey areas and yellow zones of foreign policy may create a significant risk of negative externalities. First, any response to a particular sub-federal government's foreign policy is likely to affect other sub-federal jurisdictions within the nation. Although there are examples where foreign nations have targeted retaliation against a particular sub-federal jurisdiction,<sup>67</sup> there is no guarantee that this will occur. Additionally, spill-over effects are likely even if a foreign nation attempts to so target its retaliation. Second, the federal government's foreign policy may be hindered. This can be true even if a sub-federal

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<sup>67</sup> See *id.*, at 585-86. I can think of an additional example as well. In the early 1990s, the United States retaliated against beer brewed and bottled in Ontario when that province refused to bring its laws into conformity with its GATT obligations.

government's policy seeks the same ultimate goal as the federal policy since the federal government presumably will have carefully selected the appropriate scope and degree of measures to achieve the goal. A strategy of intrusion into a grey area may also lead to clarifications by courts of the grey area to the detriment of sub-federal governments. Clear action by the federal government of its plenary power over foreign affairs could also eliminate the grey area, however, action of this type might fall within a yellow zone of political limitations. Of course, a policy of minimal intrusion by sub-federal governments is less likely to be subject to court challenge or a federal government response. Additionally, a strategy of intrusion can lead to intergovernmental frictions.

If a sub-federal government pursues a strategy of avoidance in foreign affairs, then some commentators might argue that the benefits of state autonomy, such as greater public participation in democratic rule-making and serving as laboratories of experimentation, will be diminished. However, federal foreign policy-making is no longer a very secretive process. In part, the same technological and communications revolutions that have given sub-federal policy makers certain information on conditions in foreign countries are making information available to non-governmental organizations and citizens groups. These organizations and groups have significant opportunities to influence the federal government's foreign policy. Experimentation by sub-federal governments in foreign policy will be unproductive. Such experiments are, in essence, uncontrolled since they are affected by numerous external factors, including other sub-federal foreign policies, any federal policy, and the foreign policy of other nations. Additionally, state measures are likely to be ineffective. Federal government foreign policy measures themselves can often be ineffective if undertaken unilaterally without support from other foreign countries.<sup>68</sup> Lastly, the adoption of sub-federal foreign policy measures may forestall federal government measures to address a foreign policy problem by deflecting interest group pressure from the federal government.

Nevertheless, to the extent citizens groups have greater access to sub-federal governments and sub-federal governments serve as forums that produce competing ideas, a cooperation strategy would allow for these competing ideas to be transmitted to the federal government without the negative

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<sup>68</sup> See, e.g., Gary Hufbauer & Elizabeth Winston, *Smarter Sanctions: Updating the Economic Weapon*, 7 NAT'L STRATEGY REP. 1-5 (Summer 1997) ("We suggest . . . guidelines for U.S. policy makers who find themselves considering the imposition of sanctions: recognize that sanctions alone - even severe sanctions - stand a low probability of achieving most foreign policy objectives, limit the frequency of sanctions applications by insisting on multilateral measures wherever possible . . ."). See also GARY HUFBAUER, *ECONOMIC SANCTIONS RECONSIDERED* (Inst. for Int'l. Econ., 2d ed., (1990)).

externalities resulting from a policy of intrusion. If a strategy of cooperation is pursued, intergovernmental frictions are reduced and the effectiveness of policy measures can be enhanced, for instance, if the federal government authorizes sub-federal governments to join in a sanctions regime against a foreign government.

### C. Strategies Promoting the Values of Federalism Compared with Actual Strategies Adopted

The above analysis indicated that a federal government policy of avoidance with respect to negotiating international trade and investment agreements would be the most damaging to the values of federalism. The examination also indicated that a sub-federal government's policy of intrusion with respect to foreign policy would be most damaging to the values of federalism. Unfortunately, as the analysis below reveals, the federal and state governments in the United States are increasingly utilizing the strategies that are most damaging to the values of federalism.

## VI. U.S. FEDERAL GOVERNMENT STRATEGIES FOR INTERNATIONAL TRADE AND INVESTMENT NEGOTIATIONS SEEKING TO CONSTRAIN SUB-FEDERAL GOVERNMENT POLICIES

### A. The Federal-State Clause of GATT 1947: Strategy of Avoidance or Intrusion?

The GATT 1947, which was the primary international trade agreement governing trade-in-goods until it was replaced by an updated and revised GATT 1994, contained a "federal-state clause." Through insertion of the clause, federal states sought to relieve themselves from responsibility for at least some violations committed by their sub-federal governments. To determine the extent to which the clause absolved federal governments from responsibility, it is necessary to distinguish between federal-state clauses utilizing a narrow "constitutional test" and those utilizing a broader "appropriateness test."<sup>69</sup> A federal-state clause with a "constitutional test" only relieves a federal government of responsibility in those instances in which it did not have the constitutional power to ensure sub-federal compliance. In contrast, a federal-state clause with an "appropriateness test" relieves the federal government from responsibility in all areas in which federal action to

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<sup>69</sup> Covey T. Oliver, *Enforcement of Treaties by a Federal State*, in 1974-I RECUEIL DES COURS 377, 406 (1974); Francis Maupain, *Federalism and International Labour Conventions*, 126 INT'L LABOUR REV. 625, 638 (1987). For an example of a "federal-state clause" with an appropriateness test, see CONST. INT'L LABOR ORG., art. 19(7).

ensure compliance would not be appropriate having regard for the traditional use of federal powers in the area. The GATT 1947's "federal-state clause," found in Article XXIV(12), utilized a constitutional test.

However, by utilizing such a test, federal-states, including the United States, essentially deferred selection of a strategy regarding grey areas to GATT dispute settlement panels. When disputes arose concerning sub-federal measures and federal authority to preempt the measures fell within a grey area, dispute settlement panels were left in the uncomfortable dilemma of attempting to independently assess the constitutional divisions of authority in grey areas or simply accepting the federal government's representation as to its authority. Depending on the approach of a dispute settlement panel, the federal-state clause could serve as a strategy of intrusion into a grey area or merely as a strategy of avoidance.

Several dispute settlement cases involving Canadian provincial practices and one case involving U.S. state practices forced GATT dispute settlement panels to face the question of the applicability of GATT's federal-state clause in grey areas.<sup>70</sup> The various panels differed in the extent to which they made judgments independent of the challenged government on the constitutional division of powers in grey areas.<sup>71</sup> However, in the last of the line of cases, the so-called *Beer II* case involving a Canadian retaliatory complaint against the United States regarding state practices affecting the marketing and distribution of alcohol, the GATT panel did delve into an extensive analysis of the division of powers under the U.S. Constitution, including a grey area regarding the relationship between the Commerce Clause and the 21<sup>st</sup> Amendment.<sup>72</sup> In particular, the panel extended findings of the U.S. Supreme Court regarding that relationship in the context of taxation to non-tax measures, including measures dealing with distribution. The panel found that the federal government maintained authority to legislate with respect to all measures involved in the case, including those dealing with distribution. As a result, a non-cooperative strategy of intrusion occurred since states were not extensively consulted during the negotiation of the GATT in the mid-1940s nor

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<sup>70</sup> *Canada-Taxation of Gold Coins*, GATT Doc. L/5863 (1985) [unadopted] (panel concluded that Article XXIV(12) "applies only to those [local government measures] which the federal government cannot control because [the matter] falls outside its jurisdiction under the constitutional distribution of powers"); *Canada-Measures Related to Alcoholic Beverages*, 35th Supp. BISD 37 (1988); *Canada-Import, Distribution, and Sale of Certain Alcoholic Drinks by Provincial Marketing Agencies*, 39th Supp. BISD 206 (1992); *United States-Measures Affecting Alcoholic and Malt Beverages*, 39th Supp. BISD 206 (1992) [hereinafter *Beer II*].

<sup>71</sup> *See id.*

<sup>72</sup> The panel also examined these issues in considering whether the Protocol of Provisional Application (PPA) exempted state measures existing prior to 1947 from GATT obligations. *See Beer II*, *supra* note 70, at ¶¶ 5.44-5.48, 5.78-5.80.

during the actual *Beer II* dispute in the early 1990s. As a result of the strategy of non-cooperative intrusion, federal-state frictions were created and the implementation of the panel report by the states has been quite limited. States continue to maintain many measures that the panel found to violate GATT obligations.<sup>73</sup> A more significant role for the states during the dispute settlement process may have lead to greater implementation of the panel report.<sup>74</sup>

## B. Current U.S. Federal Government Strategies

### 1. Revised Federal-state Clause of GATT 1994 and New Dispute Settlement Jurisprudence Under the GATT 1994: Strategy of Minimal Intrusion in Grey Areas and Yellow Zones

Numerous U.S. trading partners sought and succeeded in negotiating a change to GATT's federal-state clause during the Uruguay Round multilateral trade negotiations which concluded in 1994.<sup>75</sup> (Unitary states disliked the clause believing it lead to an imbalance in obligations between themselves and federal states). Specifically, the GATT 1994's Article XXIV(12) makes federal states fully responsible for violations of the GATT 1994 by their sub-federal governments.<sup>76</sup> The new Article XXIV(12) also adds that provisions relating to suspension of concessions and compensation apply where sub-federal compliance is not achieved.<sup>77</sup> The changes to Article XXIV(12) essentially remove the need for panels to delve into grey areas of the constitutional law of federations in order to determine responsibility for sub-federal violation. While obviously benefiting unitary states by removing the imbalance in obligations, the new Article XXIV(12) is also a benefit to federal states since panels are unlikely to find it necessary to engage in constitutional interpretations in grey areas. For the United States, agreeing to the new Article XXIV(12) was nearly or entirely cost free. The old GATT's federal state clause did not relieve the United States from responsibility for any obligations. The only grey area GATT obligations might implicate relates to the 21st Amendment and the *Beer II* panel already ruled that the federal-state clause did not operate to relieve the federal government from responsibility

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<sup>73</sup> See Matthew Schaefer, *Are Private Remedies in Domestic Courts Essential for International Trade Agreements to Serve Constitutional Functions?*, 17 NW. J. INT'L L. 609, 645-46 (1996/97).

<sup>74</sup> *Id.* at 646-47.

<sup>75</sup> See Matthew Schaefer, *Searching for Pareto Gains in the Relationship Between Free Trade and Federalism: Revisiting the NAFTA, Eyeing the FTAA*, 23 CAN.-U.S. L.J. 441, 464 (1997).

<sup>76</sup> Understanding on the Interpretation of Article XXIV of the GATT 1994, ¶¶ 13-15, reprinted in 33 I.L.M. 1161-63 (1994).

<sup>77</sup> *Id.*

in this area. Thus, the minimal intrusion by the federal government in the grey area created by the 21<sup>st</sup> Amendment had, in essence, already occurred as a result of the *Beer II* case.

However, a yellow zone is also implicated by GATT 1994 obligations. Most of the state autonomy restricted through the GATT was already restricted as a matter of constitutional law under the dormant Commerce Clause. The U.S. Supreme Court has interpreted the allocation of the commerce power to the federal government to serve not only as enabling the federal government to legislate with respect to economic activities having a significant effect on interstate and foreign commerce, but also as disabling the states from enacting legislation that discriminates against or unduly burdens interstate or foreign commerce.<sup>78</sup> Thus, even if the federal government refused to bind the states to the GATT, the states would face constraints on protectionist actions. Nonetheless, the anti-protectionism norms of the GATT probably differ to a small degree from those under the dormant Commerce Clause. Any movement beyond the dormant Commerce Clause in the context of an international trade agreement constitutes a yellow zone for the federal government. Numerous state interests balk at being subject to anti-protectionism constraints outside the dormant Commerce Clause. Thus, to the extent that GATT constraints differ from those of the dormant Commerce Clause, the federal government intruded into a yellow zone.

Yet, the comparison between the constraints of the dormant Commerce Clause and GATT is made difficult due to differences in opinion over what analytical method U.S. courts are truly utilizing in dormant Commerce Clause cases. The Supreme Court has developed a virtual per se rule of invalidity for facially discriminatory statutes<sup>79</sup> and appears, on the surface of its opinions, to apply a balancing test for non-facially discriminatory statutes.<sup>80</sup> In the balancing test, the Court weighs the protectionist effects of a law against the achievement of legitimate local purposes under the law.<sup>81</sup> However, there are persuasive arguments that the Courts' balancing language is mere window dressing and that, underneath the language, courts are actually searching for a protectionist motive.<sup>82</sup> Courts may be hesitant to formally and explicitly find that a state legislature has acted with an impermissible protec-

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<sup>78</sup> JOHN NOWAK & RONALD ROTUNDA, CONSTITUTIONAL LAW 281-318 (West 5th ed., (1995)).

<sup>79</sup> See, e.g., *City of Philadelphia v. New Jersey*, 437 U.S. 617 (1978).

<sup>80</sup> See *Pike v. Bruce Church, Inc.*, 397 U.S. 137 (1970).

<sup>81</sup> See *id.*

<sup>82</sup> See Donald Regan, *The Supreme Court and State Protectionism: Making Sense of the Dormant Commerce Clause*, 84 MICH. L. REV. 1091 (1986).

tionist motive, hence the window dressing.<sup>83</sup> Under this theory, the use of balancing is ultimately an attempt to snuff out a protectionist motive.<sup>84</sup>

In contrast, the GATT test appears more formalistic with an explicit text for its constraints. This may be particularly true since WTO dispute settlement panels are directed to use customary international law rules of interpretation that place primary emphasis on the text of treaty obligations.<sup>85</sup> Nonetheless, it is quite possible that GATT panels are influenced by the apparent protectionist motive (or lack thereof) behind the measures they examine.<sup>86</sup> GATT's national treatment obligations require that a state treat a product from Member countries "no less favorably" than an in-state "like product" with respect to domestic regulations and that a state not tax a foreign "like product" in excess of its domestic counterpart.<sup>87</sup> One study in 1994 found a remarkable similarity in approach between dormant Commerce Clause jurisprudence and GATT's approach.<sup>88</sup> However, that study was made during the time of the so-called "aims and effects" test for determining like products. Under the aims and effects test, products are not "like" if an origin-neutral regulatory distinction between the products does not have the aim or effect of affording protection.<sup>89</sup> The aims and effects test made review under GATT's national treatment obligation quite similar to the approach under the dormant Commerce Clause. However, the aims and effects test is (apparently) dead under the GATT 1994 – at least with respect to taxation measures.<sup>90</sup> Instead, GATT 1994 jurisprudence emphasizes the so-called traditional approach of determining like products that includes looking at the following factors: "the product's end-uses in a given market; consumers' tastes and habits . . . ; the product's properties, nature and quality."<sup>91</sup>

Thus, the similarity between the two doctrines has likely decreased somewhat as a result of the death of the aims and effects test. However, the current differences should not be overstated. First, it is possible that the tra-

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<sup>83</sup> *Id.* at 1093.

<sup>84</sup> *Id.* at 1284-86.

<sup>85</sup> See Understanding on Rules and Procedures Governing the Settlement of Disputes, reprinted in 33 I.L.M. 1226 (1994), art. 3(2).

<sup>86</sup> See Daniel Farber & Robert Hudec, *Free Trade and the Regulatory State: A GATT's-Eye View of the Dormant Commerce Clause*, 47 VAND. L. REV. 1401 (1994).

<sup>87</sup> GATT 1994, arts. III(4) & III(2).

<sup>88</sup> Farber & Hudec, *supra* note 84.

<sup>89</sup> *United States-Taxes on Automobiles*, reprinted in 33 I.L.M. 1397 (1994) (unadopted by GATT Council), ¶¶ 5.7-5.55; *Beer II*, *supra* note 70, at ¶¶ 5.70-5.77.

<sup>90</sup> See *Japan - Taxes on Alcoholic Beverages*, WTO Doc. WT/DS8/AB/R (Oct. 4, 1996) at 19-22, modifying *Japan - Taxes on Alcoholic Beverages*, WTO Doc. WT/DS8/R (July 11, 1996) at ¶¶ 6.14-6.22, available on WTO website <<http://www.wto.org>> (visited on July 6, 1998).

<sup>91</sup> See *id.* at 19-22.



ditional like products analysis would uphold the regulatory distinctions upheld in the two GATT 1947 dispute settlement panel reports that relied on the "aims and effects" test. For instance, in the so-called GATT *Beer II* dispute settlement case discussed above, the panel found that low-alcohol and high-alcohol beer were not like products and thus could be taxed at different rates because the "aim and effect" of the measure was not to afford protection.<sup>92</sup> The differences in alcoholic content could be significant under traditional like products analysis as well, particularly since there is little competition between high and low-alcohol beer which indicates differences in consumer tastes. Moreover, even if a state measure should violate the national treatment obligation, it may still not violate the GATT if it can be justified under the general exceptions clause of the GATT.<sup>93</sup> The general exceptions clause allows, for example, measures "necessary to protect human, animal and plant life or health."<sup>94</sup> "Necessary" has been interpreted to require the "least-trade-restrictive" alternative.<sup>95</sup> While GATT jurisprudence has been criticized for the least-trade restrictive test, U.S. constitutional commentators have described tests the Supreme Court applies in similar terms.<sup>96</sup>

Since the constraints the states face under the so-called "dormant Commerce Clause" do not overlap in every respect with anti-protectionism obligations found within the GATT, the federal government has intruded into a yellow zone. However, this intrusion is minimal. While it is possible to identify situations in which a state measure is treated more favorably under the dormant Commerce Clause than those found within the GATT, it is also possible to identify instances in which the GATT is more lenient.<sup>97</sup> But the more critical point is that the dormant Commerce Clause does not necessarily represent the appropriate line that should be drawn with respect to state auton-

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<sup>92</sup> *Beer II*, *supra* note 70, at ¶¶ 5.70-5.77.

<sup>93</sup> GATT 1994, art. XX.

<sup>94</sup> GATT 1994, art. XX(b).

<sup>95</sup> *See, e.g., Thailand - Restrictions on the Importation of and Internal Taxes on Cigarettes*, BISD, 37th Supp. at 200 (adopted Nov. 7, 1990).

<sup>96</sup> NOWAK & ROTUNDA, *supra* note 78, at 298.

<sup>97</sup> For an example of GATT constraints being more lenient than the dormant Commerce Clause, compare GATT 1994, art. III:8 (allowing payments directly to producers even if payments are derived from taxes on both imported and domestic products) with *West Lynn Creamery, Inc. v. Healy*, 512 U.S. 186 (1994) (invalidating subsidy to in-state milk producers paid directly from tax on all sales of milk, including out-of-state milk, to retailers). Note, however, that a separate Uruguay Round agreement dealing with subsidies places certain minimal constraints on state subsidies to industry. For a possible example of dormant Commerce Clause constraints being more lenient than the GATT, compare *Beer II*, *supra* note 70, at ¶ 5.19 (holding that Minnesota law giving excise tax break to beer brewed by microbreweries wherever located violated GATT Article III's national treatment obligation) with claim by state tax administrators that such a law would withstand dormant Commerce Clause scrutiny. *See Schaefer*, *supra* note 75, at 459.

omy. The federal government implicitly recognized this point by agreeing to bind the states to the standards in GATT and thus intrude into a yellow zone. (Admittedly, the degree of intrusion is ultimately determined by the new jurisprudence in dispute settlement cases under the GATT 1994.) Yet, to date, the federal government is less willing to recognize in the context of agreements dealing with trade-in-services and investment that existing constitutional constraints do not maximize the values of federalism.

## 2. "Grandfathering" of Existing Measures in Trade-in-Services and Investment Agreements: Strategy of Avoidance of a Yellow Zone

In this decade, international trade agreements, including the Uruguay Round agreements and the North American Free Trade Agreement (NAFTA) have expanded to address "new" issues, such as trade-in-services and investment. Obligations regarding these "new" issues potentially increase the impact of international trade agreements on sub-federal governments because of the significant regulatory and enforcement authority that sub-federal governments exercise in the area of services and investment. However, these expanded obligations within international trade agreements do not touch upon grey areas within the split sovereignty of the United States. The anti-protectionism obligations of trade agreements do not enter into the judicially imposed outer limits of federal legislative power under the Commerce Clause.<sup>98</sup> The federal government has the constitutional power to restrict discriminatory state regulations affecting trade-in-services and foreign investment.

However, the U.S. federal government is confronted with a yellow zone in the negotiation and implementation of international agreements in the new areas of trade-in-services and investment.<sup>99</sup> The U.S. strategy as regards this yellow zone has been to pursue the near equivalent of a federal-state clause with an appropriateness test in services and investment negotiations. Specifically, the NAFTA exempted all existing state measures that conflicted with major anti-protectionism obligations of the services and investment chapters in the agreement.<sup>100</sup> In other words, such measures are "grandfathered."<sup>101</sup>

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<sup>98</sup> See Schaefer, *supra* note 64.

<sup>99</sup> See Schaefer, *supra* note 75, at 456-58.

<sup>100</sup> See North American Free Trade Agreement, *reprinted in* 32 I.L.M. 639 (1993), arts. 1108(1), 1206(1). Originally, sub-federal measures were required to be identified and listed in an annex in order to be exempted from coverage. However, due to problems in the identification process, the NAFTA parties agreed to exempt all existing non-conforming measures without identifying and listing specific measures. See *NAFTA Partners to Protect Sub-Federal Measures from NAFTA Challenges*, INSIDE U.S. TRADE, Apr. 5, 1996, at 1. See also Schaefer, *supra* note 75, at 469-71.

<sup>101</sup> Schaefer, *supra* note 75, at 469-71.

This grandfathering technique is also utilized by the federal government in broader multilateral negotiations related to trade-in-services and investment. The General Agreement on Trade in Services (GATS) effectively exempts existing non-conforming state measures from coverage.<sup>102</sup> The Multilateral Agreement on Investment (MAI), currently being negotiated by the twenty-nine nations of the Organization for Economic Cooperation and Development (OECD), will also likely exempt from coverage existing state measures that would conflict with major obligations.<sup>103</sup>

By exempting all existing state measures from the major anti-protectionism obligations in these agreements, the U.S. federal government is starting the liberalization of state-level services trade and investment restrictions at a worse point than it did fifty years ago with respect to trade-in-goods in the original GATT 1947.<sup>104</sup> And the original GATT 1947's federal-state clause was negotiated in an era in which the implications of the federal government's expanded commerce power were perhaps less clear.

But is the current U.S. strategy to avoid a yellow zone actually justified as necessary to preserve the values of local autonomy within a federation, particularly when the U.S. approach to trade-in-goods is much more aggressive? For instance, two of the primary types of "grandfathered" state restrictions affecting trade-in-services and investment are citizenship and residency requirements. While these requirements act as a barrier to trade-in-services and investment, they do not further the values of federalism. Such restrictions are essentially beggar-thy-neighbor policies which are responded to in kind by foreign trading partners. Such requirements do not protect consumers or health and welfare (or at the very least there are less restrictive means of achieving such goals). Such requirements also do not represent useful experiments since protectionism is a failed experiment.

As noted above in the context of the GATT dealing with trade-in-goods, a yellow zone exists for any obligations created by international agreements that extend beyond existing U.S. constitutional constraints on the states, including the dormant Commerce Clause. One possible reason for the U.S.

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<sup>102</sup> General Agreement on Trade in Services, *reprinted in* 33 I.L.M. 1168 (1994), art. XVII(1) (allowing nations to condition and qualify the extent to which the national treatment obligations applied to listed service sectors).

<sup>103</sup> See *Larson Casts Doubt on Ability to Conclude MAI; Sets No Timeline*, INSIDE U.S. TRADE, Mar. 13, 1998, at 11 ("... the U.S. is seeking ... to protect existing state and local measures that may not conform to the MAI once it is completed").

<sup>104</sup> The Protocol of Provisional Application (PPA) by which GATT was applied exempted existing federal measures not conforming with GATT obligations (except Articles I and II) if the Executive did not have authority to change the measure. The PPA did not provide an exemption for GATT-inconsistent state measures existing as of 1947 since the Executive, via Congressional delegation, had authority to preempt such measures. See *Beer II*, *supra* note 70, at ¶¶ 5.44-5.48.

failure to intrude on the yellow zone with respect to trade-in-services and investment may be that the international trade agreement constraints dealing with trade-in-services and investment extend beyond existing constitutional constraints, such as the dormant Commerce Clause, to a greater degree than with trade-in-goods. Again, however, the dormant Commerce Clause jurisprudence does not necessarily represent the ideal limits on state autonomy. Moreover, other clauses of the Constitution, such as the Equal Protection Clause<sup>105</sup> and Privileges and Immunities Clause<sup>106</sup> have been utilized by the courts to invalidate citizenship, residency, and other protectionist laws affecting trade-in-services and investment.<sup>107</sup> Indeed, some of the measures "grandfathered" under trade agreements may be constitutional violations.

Naturally, there may be some measures so essential to state autonomy that they must be immunized from challenge under trade and investment agreements because the general exceptions clauses of these agreements do not appropriately recognize pursuit of the objective. Additionally, state laws may need to be immunized from the introduction of stringent harmonization obligations in international trade agreements,<sup>108</sup> however, trade agreements are unlikely to introduce such obligations. With these caveats, however, binding the states more fully to obligations within current international agreements governing trade-in-services and investment will advance rather than harm the values of federalism.

Thus, the avoidance strategy of the federal government can only be justified as a short-term policy if a strategy of cooperation is pursued to induce further liberalization.<sup>109</sup> A cooperation strategy, like the avoidance strategy, reduces federal-state frictions. However, the cooperation strategy will at least seek the elimination of state autonomy to enact beggar-thy-neighbor policies. Nonetheless, the bargaining that occurs under a cooperation strategy may fail to yield significant results if states perceive that avoidance will continue as the federal government's strategy should cooperation fail. The Government Procurement Agreement, re-negotiated during the Uruguay Round, provides

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<sup>105</sup> U.S. CONST., amend. XIV (applying to persons).

<sup>106</sup> U.S. CONST., art. IV, § 2 (applying to citizens).

<sup>107</sup> See, e.g., *Yick Wo v. Hopkins*, 118 U.S. 356 (1886) (invalidating under Equal Protection Clause measures that denied resident Chinese aliens licenses to operate laundries); *In Re Griffiths*, 413 U.S. 717 (1973) (invalidating under Equal Protection Clause a citizenship requirement to sit for a state bar exam); *Metropolitan Life Ins. Co. v. Ward*, 470 U.S. 869, 881-882 (1985) (invalidating under Equal Protection Clause a protectionist state insurance measure); *Supreme Court of New Hampshire v. Piper*, 470 U.S. 274 (1985) (invalidating under Privileges and Immunities Clause a requirement that one be a resident prior to joining the state bar).

<sup>108</sup> See Schaefer, *supra* note 75, at 476-77.

<sup>109</sup> With respect to current and potential cooperation mechanisms, see Schaefer, *supra* note 75, at 479-83.

such an example. The federal government decided to bind state procurement to anti-protectionism and other obligations within the GPA on a voluntary basis.<sup>110</sup> Specifically, the U.S. government's approach to the negotiations with respect to state governments was to bind a particular state only if a voluntary commitment to be bound was submitted by that state's governor, and only to the extent reflected in that voluntary commitment.<sup>111</sup> The federal government sought to educate the states on the benefits of liberalized procurement policies and the reciprocal liberalization that would be achieved in foreign procurement markets for U.S. suppliers. Nonetheless, the cooperative approach only lead to a "standstill" against new state protectionism in thirty-seven states.<sup>112</sup> No state made a voluntary commitment that liberalized existing state procurement preferences and thirteen states refused to make any commitment at all. Therefore, thirteen states maintain complete freedom to enact further protectionist procurement laws in the future. Accordingly, a more aggressive strategy of cooperation may need to be instituted to further the values of federalism.

#### VII. STATE GOVERNMENT STRATEGIES WITH RESPECT TO FOREIGN POLICIES

U.S. state activity in foreign affairs is growing as a result of globalization. Yet, the strategies states have chosen in response to globalization differ with respect to various grey areas exposed by globalization.

In a global economy, attraction of foreign investment can have a significant impact on state economic conditions and employment. In such an environment, states have incentives to disseminate information on business climate conditions. Therefore, as mentioned previously, states have established overseas investment offices that seek to attract foreign investment. Similarly, in a global economy taking advantage of new markets is important to state economic conditions and employment. Accordingly, state governors routinely organize trade missions seeking to enhance contacts between producers operating within the state and potential foreign buyers. As discussed previously, such activity, at least as a general matter, likely does not fall within any grey areas of the division of authority between federal and state governments despite the power granted to the President to send and receive ambassadors and the prohibition on states entering into compacts with foreign governments. The primary goal of such offices and missions is to establish contacts with potential foreign investors and potential purchasers for state ex-

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<sup>110</sup> *Id.* at 472-73.

<sup>111</sup> *Id.*

<sup>112</sup> *Id.* at 488.

porters. States generally inform and cooperate with federal agencies and embassies when engaging in this type of conduct so as to avoid stretching their conduct into an area of federal responsibility. Thus, the states' strategy pertaining to the narrow band of grey surrounding overseas trade and investment offices and trade missions has largely been one of avoidance and cooperation. State activity in the field of negotiation and conclusion of agreements is also undertaken in a cooperative manner by generally notifying the federal government.<sup>113</sup> To date, state activities with respect to negotiations and agreements generally do not lead to policies that cause negative externalities for other states or beggar-thy-neighbor policies.

Strikingly, the strategies of cooperation and avoidance chosen by states with respect to overseas offices, trade missions, agreements, and negotiations are not being followed within a much more significant grey area exposed by globalization. This grey area relates to the enactment by states of foreign policy legislation, particularly legislation seeking to sanction certain foreign governments. Increased information and communication flows have increased awareness of state government officials and local citizens groups of conditions in foreign countries. Increased trade and investment flows give states at least some reason to believe that they maintain a significant lever to influence policies of foreign governments. As a result, state sanctions legislation with a foreign policy motive, particularly with respect to human rights, is rapidly increasing. Such legislation was prevalent during the mid-1980s with respect to South Africa. For instance, many states passed laws that required state pension funds to divest holdings in South Africa, prevented the state from procuring goods of South African origin, granted procurement preferences to those entities that refused to deal with South Africa, and/or accorded discriminatory tax treatment to South African currency.<sup>114</sup> A few such laws were challenged on the basis of the dormant foreign affairs doctrine and/or as being preempted by federal sanctions legislation.<sup>115</sup> The outcome of such cases varied<sup>116</sup> and none of the cases worked their way up to the Supreme Court. Accordingly, as noted previously, a grey area remains regarding state foreign affairs legislation where the federal government has not explicitly preempted the states. Only a few cases were brought because

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<sup>113</sup> Kincaid, *supra* note 38, at 131, 137.

<sup>114</sup> See Bilder, *supra* note 48, at 822; Howard Fenton, *The Fallacy of Federalism in Foreign Affairs: State and Local Foreign Policy Trade Restrictions*, 13 *Nw. J. INT'L & BUS.* 563, 568-71 (1992).

<sup>115</sup> Board of Trustees v. City of Baltimore, 562 A.2d 720 (Md. 1989) (upholding city ordinances requiring that city pension funds divest their holdings in companies doing business in South Africa); Springfield Rare Coins Galleries v. Johnson, 503 N.E.2d 300 (Ill. 1986) (striking down discriminatory sales tax on South African currency).

<sup>116</sup> See *id.*

such litigation can be costly for private plaintiffs, both in terms of legal expenses and possible bad publicity if they are viewed as supporting a rogue regime in a foreign country. Private plaintiffs generally gave these costs greater weight than the potential benefits of challenging the state legislation since the likelihood of success in such a case was uncertain as a result of questions concerning the scope of the dormant foreign affairs doctrine and the preemptive effect of federal sanction laws.

While a few years of relative calm prevailed in terms of state "foreign affairs" sanction legislation after apartheid was eliminated in South Africa, such activity is multiplying. Such legislation is currently focused on Burma or Myanmar, a country ruled by an undemocratic military regime and maintaining a poor human rights record. The State of Massachusetts is probably the largest sub-national economic actor maintaining sanctions with the goal of changing conditions in Burma. Massachusetts maintains a procurement law that prevents the state from procuring goods or services from companies active in Burma unless it would result in inadequate competition. In operation, the statute results in a company active in Burma having ten percent added to its bid prior to the determination of the low bidder.<sup>117</sup> Numerous other states and localities have adopted, or are in the process of considering, similar laws with respect to Burma. Many states and localities are also considering sanctions legislation with respect to companies active in Nigeria and other undemocratic regimes.<sup>118</sup>

The states are thus following a strategy of significant and increasing intrusion into this grey area. This strategy has created some conflict between the United States and its trading partners, including the European Community and Japan. Indeed, trading partners have threatened to bring a WTO dispute settlement case based on the Government Procurement Agreement if the Massachusetts law is not amended such that it would only apply to contracts below a threshold established in the agreement.<sup>119</sup> The friction between the federal government and Massachusetts remains muted, largely because the federal government has been exceedingly deferential to the Massachusetts measure despite the existence of federal sanctions legislation against Burma that only seeks to prevent new investment rather than eliminate current investment in Burma.<sup>120</sup> The federal government has simply attempted gentle

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<sup>117</sup> See *Lawmaker Offers Change to State Law for U.S., E.U. Promises on Burma*, INSIDE U.S. TRADE, Apr. 24, 1998, at 1-2.

<sup>118</sup> See Jim Lobe, *Lawsuit Filed on U.S. State Sanctions Against Burma*, INTERPRESS SERVICE, May 1, 1998, available in 1998 WL 5986992; Evelyn Iritani, *Coalition Challenges Myanmar Trade Ban in Court*, L.A. TIMES, May 1, 1998, at D1.

<sup>119</sup> See *EU Threatens WTO Panel Without Quick End to State Sanctions Fight*, INSIDE U.S. TRADE, Mar. 20, 1998, at 1.

<sup>120</sup> See Exec. Order No. 13047, 62 Fed. Reg. 28301 (1997).

persuasion with Massachusetts in order to have the law amended so as to not apply to contracts governed by the Government Procurement Agreement. The federal government has not sought removal of the law in its entirety.

In addition to the influence of globalization, increased activity in this grey area may result from several political factors. First, state politicians see such measures as "good politics."<sup>121</sup> In the current political climate, state politicians gain local political benefits from upstaging the U.S. State Department. Moreover, the costs of such actions are borne largely from those outside the state and/or dispersed in-state interests (e.g. the taxpayers who foot a larger bill for state procurement). Second, based in part on their experiences with sanctions against South Africa, state politicians believe that the federal government will not explicitly preempt such measures as a result of "state sovereignty" political concerns and that private parties will continue to be hesitant to challenge such measures.

The states' calculation with respect to the federal government appears correct. The federal government views explicit preemption of state foreign affairs legislation to fall within a yellow zone.<sup>122</sup> However, the appropriate question is whether this yellow zone protects some benefits of state autonomy in a federal system? State foreign policies lead to significant potential externalities and the creation of negative externalities is a strong justification for federal intervention. Any overt retaliation by aggrieved foreign nations or even subtler forms of damage to U.S. foreign policy is likely to fall upon the nation as a whole. Even if a foreign government decides to retaliate and attempts to target retaliation at entities located within the particular state adopting a sanctions law, spill-over effects to other states are likely. With the federal political branches refusing to enter a yellow zone, despite the fact the yellow zone does not reflect a concern over the values of state autonomy sought through federalism, it is left to businesses to challenge such legislation and ultimately courts to resolve the grey area that remains in the absence of explicit federal preemption.

Indeed, the state strategy of intrusion undoubtedly would continue to be successful, not in achieving the changes in foreign government policy they seek, but in aggrandizing the power of the states and providing political benefits for state politicians, were it not for the ability of private business interests to finally overcome collective action problems of their own. The

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<sup>121</sup> See, e.g., *The Mass That Roared*, THE ECONOMIST, Feb. 8, 1997, at 32-33 (" . . . in the middle of his campaign last year to nab the [U.S.] Senate seat of John Kerry, [Governor] Weld noticed that Mr. Kerry had been slow to endorse sanctions on Myanmar [i.e. Burma]. Mr. Weld got religion. Last June 25th, flanked by Burmese activists, Mr. Weld signed the bill"). See also Fenton, *supra* note 114, at 590.

<sup>122</sup> See, e.g., Fenton, *supra* note 114, at 591-92.



National Foreign Trade Council (NFTC), a coalition of businesses of which thirty are on the Massachusetts Burma law's restricted list, has filed suit in federal court seeking to have the Massachusetts's Burma law ruled unconstitutional.<sup>123</sup> The NFTC's claim is that Massachusetts's Burma law is impliedly preempted by existing federal sanctions against Burma and that, even if federal sanctions legislation does not preempt the state action, the dormant foreign affairs doctrine prohibits the state law.<sup>124</sup> By acting in a coalition, the businesses are able to overcome a "free rider"-type situation in which businesses wait for each other to challenge the law. First, by acting in a coalition, businesses are able to share the costs of litigation. Second, any bad publicity will be spread among many entities and utilizing an organization name will further reduce any potential consumer backlash. While the likelihood of success is not certain, the judgment was made that the costs of the legislation to businesses, particularly in light of the proliferation of similar laws, was great enough to proceed. Even if the suit fails, the businesses can argue forcefully that the Congress must always consider the issue of explicit preemption of state sanctions when it passes federal sanctions legislation. In the current state of grey, the Congress can respond to businesses that Congress need not explicitly address the issue in legislation since the Constitution already prohibits such action and then leave it too businesses to seek enforcement of the grey constitutional constraints.

Thus, it is possible the grey area of state-level foreign affairs activity will be clarified in the next few years. However, it is by no means certain since the court might strike down the Massachusetts law on rather narrow grounds or, alternatively, dismiss the case due to standing problems.<sup>125</sup> Therefore, conscientious politicians willing to weigh the values of federalism are required to promote the values of federalism by changing state strategies of intrusion to strategies of cooperation and avoidance. There are some early indications that the federal government is gradually shifting to a more proac-

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<sup>123</sup> See *NFTC Launches Constitutional Challenge Against State Sanctions*, INSIDE U.S. TRADE, May 1, 1998, at 1, 23.

<sup>124</sup> See *id.* See also *USA-Engage Announces Constitutional Challenge of State Law*, INSIDE U.S. TRADE, Feb. 13, 1998, at 3-4. Note that an additional claim raised by plaintiffs is that the Massachusetts law violates the dormant Foreign Commerce Clause.

<sup>125</sup> For instance, the court may invalidate the law on the basis of the dormant Foreign Commerce Clause by ruling that the state law does not meet the market participant exception. See, e.g., *South-Central Timber Development v. Wunnicke*, 467 U.S. 82, 97 (1984) (In order to meet the market participant exception, a "State may not impose conditions, whether by statute, regulation or contract, that have a substantial regulatory effect outside of that particular market"). As a result, the court may not eliminate the grey area surrounding the dormant Foreign Affairs Doctrine.

tive strategy of "aggressive cooperation" to ward off future state measures of this type.<sup>126</sup>

### VIII. COMPARISON TO CANADIAN STRATEGIES

The strategies pursued in response to globalization by the U.S. federal government and state governments can be compared with those of their Canadian counterparts. The comparison further highlights the misguided "new federalism" apparent in the strategies pursued by the various levels of government in the United States.

#### A. Grey Areas in Canadian Federalism

##### 1. External Affairs

At the time Canada federated, it was a dominion of the United Kingdom such that its external affairs were handled by the United Kingdom.<sup>127</sup> As a result, the Canadian Constitution has only one provision regarding treaties and that provision has been read out of existence by judicial interpretation.<sup>128</sup> Accordingly, it is perhaps not a surprise to find that questions regarding the legal division of authority between the federal and provincial authorities with respect to treaty-making linger (although currently latent) and that the division of authority regarding treaty implementation is colored by significant grey.

The federal government maintains it has an exclusive treaty-making power.<sup>129</sup> While some provinces have been willing to recognize exclusive federal treaty-making capacity, at least one province, Quebec, still maintains that it has the power to enter into treaties (agreements governed by interna-

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<sup>126</sup> Indeed, the officials of the United States Trade Representative's office recently met with the NGA to urge states to consult with the USTR before considering sanctions legislation. See *USA-Engage Announces Constitutional Challenge of State Law*, INSIDE U.S. TRADE, Feb. 13, 1998, at 3-4. However, it appears such consultations will focus on having state sanctions proposals conform with the Government Procurement Agreement, rather than the wisdom of such sanctions legislation in terms of the values of federalism. Nevertheless, the federal government apparently had a role in warding off sanctions being considered by the Maryland legislature against Nigeria.

<sup>127</sup> See PETER HOGG, *CONSTITUTIONAL LAW OF CANADA*, §§1.1, 11.2 (Carswell 3rd ed., looseleaf, 1992).

<sup>128</sup> That provision being British North American Act, subsequently renamed the Constitution Act of 1867, § 132.

<sup>129</sup> See, e.g., Debra Steger, *Canadian Implementation of the Agreement Establishing the World Trade Organization*, in *IMPLEMENTING THE URUGUAY ROUND* 243, 261 (John Jackson & Alan Sykes eds. (1997)) ("Treaty-making is also an exclusively federal power . . . . The federal government has never accepted the existence of [a provincial treaty-making] power").

tional law).<sup>130</sup> However, attempts by Quebec in the 1960s to enter into agreements with France and other foreign nations that might be governed by international law and dealing with cultural, educational, and technical cooperation created significant controversy.<sup>131</sup> The federal government has been vigilant in ensuring that its assent was given to the most important of these arrangements prior to their conclusion.<sup>132</sup> The assent has come in the form of an exchange of notes between federal governments, the establishment of a general framework agreement with the other government providing that provinces could enter into such arrangements, or the passage of an Act of Parliament.

## 2. Internal Affairs

The Canadian Constitution, in contrast to the U.S. Constitution, grants legislative powers to the provinces and leaves the residual powers to the federal government, explicitly stating some of the powers that this residual encompasses.<sup>133</sup> The federal government is granted the power to make laws for "peace, order and good government," including laws relating to "trade and commerce."<sup>134</sup> However, the trade and commerce power, which reads quite similar to its U.S. counterpart, has been narrowly interpreted by the courts so as to protect provincial jurisdiction.<sup>135</sup> The most significant provincial power arises from the grant of the power over "property and civil rights."<sup>136</sup> This head of power gives provinces significant regulatory authority over the professions, insurance, securities, and other service-related industries.<sup>137</sup> It also gives power to the provinces with respect to expropriation and other investment-related issues.<sup>138</sup> Whether a particular piece of legislation fits within a federal or provincial head of power can be controversial. Canadian courts

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<sup>130</sup> See, e.g., J.V. Morin, *International Law, Treaty Making Power, Constitutional Law, Position of the Government of Quebec*, 45 CAN. BAR. REV. 160 (1967).

<sup>131</sup> See, e.g., Edward McWhinney, *Canadian Federalism, and the Foreign Affairs and Treaty Power: The Impact of Quebec's Quiet Revolution*, 1969 CAN. Y.B. INT'L L. 4-5.

<sup>132</sup> See, e.g., Gerald Fitzgerald, *Educational and Cultural Agreements and Ententes of France, Canada and Quebec: Birth of a New Treaty Making Technique for Federal States*, 60 AM. J. INT'L L. 529 (1966).

<sup>133</sup> British North American Act, subsequently renamed the Constitution Act 1867, §§ 91-92.

<sup>134</sup> *Id.*, art. 91.

<sup>135</sup> See John D. Whyte, *Federal Powers Over the Economy: Finding New Jurisdictional Room*, 13 CAN. BUS. L.J. 257, 259 (1988) (noting that "federalism has been the political idea that has attracted the highest level of judicial respect").

<sup>136</sup> See HOGG, *supra* note 127, at 537.

<sup>137</sup> *Id.* at §§ 21.5, 21.7, 21.10.

<sup>138</sup> *Id.* at §§ 21.11, 28.5.

undertake a two-step process: first, they characterize the law as dealing with a particular matter, and second, they determine whether that matter falls within a provincial or federal head of power after interpreting the scope of various heads of power.<sup>139</sup> As a result of the Canadian constitutional structure and interpretations, the grey areas are more prominent in the Canadian federation as compared with the United States in regards to legislative powers of the federal and sub-federal governments.

In Canada, the power of the federal government to implement international trade agreement obligations applicable to the provinces is not assured. Under the famous *Labor Conventions* case,<sup>140</sup> the Privy Council ruled that the federal government did not have a broad treaty implementing power, rather legislation implementing a treaty would have to be justified under a specific head of power granted to the federal government in the Constitution. If the subject matter of an obligation within an international agreement fell within a provincial head of power under the Constitution rather than a federal head of power, then the provinces alone would have the authority to implement the obligation.<sup>141</sup> However, the Supreme Court of Canada has at times hinted at dissatisfaction with the *Labor Conventions* rule.<sup>142</sup> Moreover, the Court has potentially expanded the trade and commerce power and "peace, order and good government" clause enough to support trade agreement implementing legislation.<sup>143</sup> Indeed, many Canadian commentators speculated that the federal government would have been victorious in a jurisdictional case that probably would have arisen had the Canadian government taken an aggressive posture with respect to legislation implementing the Canada-U.S. Free Trade Agreement in the late 1980s. However, by the time the Canada faced implementation of the North American Free Trade Agreement and the Uruguay Round Agreements in the early and mid-1990s, commentators felt less certain that the court would be as solicitous given the climate of the Canadian federation.

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<sup>139</sup> *Id.* at §§ 15.4-15.5; Steger, *supra* note 129, at 266.

<sup>140</sup> *A.G. Canada v. A.G. Ontario* [1937] AC 326.

<sup>141</sup> *Id.* at 351. *See also* Steger, *supra* note 129, at 267.

<sup>142</sup> *See* HOGG, *supra* note 127, § 11.5(c).

<sup>143</sup> Regarding the possibilities of federal government using the "trade and commerce" power or the "peace, order and good government" clause to implement trade agreement obligations in the grey areas, see Debra Steger, *supra* note 129, at 270-76.

## B. Current Canadian Strategies

### 1. Federal Government Strategy With Respect to International Trade and Investment Agreements

Any attempt to bind provinces fully to the trade-in-services and investment obligations within international agreements might expose grey areas in Canada's split sovereignty to a significant degree. Again, the provincial head of power related to "property and civil rights" gives provinces significant regulatory authority over numerous services sectors, including professional services, insurance, and securities. However, the technique of "grandfathering" of existing non-conforming measures within NAFTA and the exemption of listed non-conforming measures in the GATS has minimized any intrusion, or at least immediate intrusion, into these grey areas.<sup>144</sup>

Nonetheless, with respect to certain obligations, the provinces are fully bound and current provincial law may conflict with obligations within international trade agreements. For instance, the Canadian federal government made no reservation for provincial measures inconsistent with NAFTA's provisions regarding expropriation of foreign investments. NAFTA's standards for what constitutes expropriation may be broader than those under current provincial law and its standards for compensation may differ from those provided under provincial law. The provincial head of power related to "property and civil rights" encompasses expropriation matters and thus a jurisdictional case could arise in this area. The Canadian government pursued minimal intrusion to reduce the likelihood of a jurisdictional case being brought to the courts, but it believed that it maintained at least a fair chance of success in any such a challenge in light of new jurisprudence under the "trade and commerce" power and the "peace, order and good government" clause. However, it is likely that any further intrusions will have to be preceded by a cooperative strategy since the federal government is not necessarily anxious to press for a court case.

The U.S. strategy of avoidance of a yellow zone contrasts with the Canadian strategy of minimal intrusion into a grey area. The U.S. federal government strategy can only be justified if liberalization of provincial and state restrictions on services and investment will need to occur reciprocally. In other words, since the yellow zone faced by the U.S. federal government does not relate to any values sought to be promoted by federalism, the only legitimate reason for the U.S. federal government to pursue a strategy of

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<sup>144</sup> The minimalist approach in the respective implementing bills of NAFTA and the Uruguay Round Agreements also minimizes any immediate intrusion. See Anonymous, *Issues of Constitutional Jurisdiction, in Canada: The State of the Federation* 39, 45-46 (1987-88 ed.); Schaefer, *supra* note 73, at 642-43.

avoidance to date is the existence of analogous Canadian provincial restrictions. However, the Canadian government is unlikely to launch a campaign of "aggressive cooperation" until the U.S. government takes the lead in adopting such a strategy to eliminate remaining beggar-thy-neighbor policies at the state level.

## 2. Canadian Provincial Strategies with Respect to Foreign Affairs Legislation

The Canadian provinces have not enacted foreign affairs sanctions legislation such as the Massachusetts Burma law. The lack of such legislation may result from the lack of grey with respect to such authority, i.e., the legal authority of a province to enact such a measure may well be denied by the Canadian constitution. Such a law is not likely to be characterized as relating to a matter within a provincial head of power.<sup>145</sup> Alternatively, the provinces are simply showing greater restraint in the area of unilateral sanctions and instituting a policy of avoidance recognizing that provincial action, let alone federal action, is likely to be ineffective and create possible negative externalities. In either case, it is striking that the Canadian system operates in a manner in which such activity is not undertaken at the sub-federal level when most observers view the Canadian federation as maintaining more significant grey in the realm of foreign affairs as compared to the United States.

## IX. CONCLUSION

Globalization is not a threat to U.S. federalism. Rather, the choice of strategies by governments in the United States in response to globalization threatens the values that federalism seeks to promote. Indeed, the choice of strategies by governments in the United States reveals that the renewed calls for a "new federalism" may have gone awry. The federal government strategy with respect to globalization allows for state autonomy, and states are utilizing such autonomy, to adopt beggar-thy-neighbor policies, policies that create potentially significant negative externalities, and other inefficient policies resulting from prisoner's dilemma-type situations. Moreover, the benefits of state autonomy, such as acting as laboratories for experimentation and providing potentially greater public participation in democracy, are not promoted through the strategies adopted by governments in the United States in response to globalization.

Examining the strategies chosen by governments in Canada in response to grey areas and yellow zones exposed by globalization lends further sup-

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<sup>145</sup> Discussion with anonymous Canadian law professor at American Society of International Law's 1998 Annual Meeting. Any error in the text is my responsibility.

port to the conclusion that “new federalism” with the United States is in danger of proceeding down a mistaken path. Canada’s federal government is following a policy of minimal intrusion into grey areas with respect to trade negotiations and Canada’s provinces are pursuing a strategy of avoidance with respect to sanctions legislation for foreign policy purposes. These strategies instituted by governments in what many consider a less centralized and less stable federation in which the division of powers is subject to more significant grey areas are arguably in stark contrast to those being pursued by governments in the United States.

Business may seek to rescue (for their own benefit) the governments of the United States from their misguided implementation of a “new federalism” reflected in the strategies they choose in response to globalization. Businesses may do so by lobbying the federal government to seek further state liberalization of trade and investment policies and by challenging state foreign affairs sanctions legislation in the courts. However, policing by businesses in these areas is unlikely to be a complete success. Moreover, while businesses can serve a limited policing role for “new federalism” in the area of trade negotiations and foreign policy, businesses may have motives adverse to an appropriate “new federalism” in other areas of governmental regulation. A process engaged in by businesses alone cannot ensure the proper roles for federal and state government in “new federalism.” Nor can courts ensure the proper division of exercised authority between federal and state governments. Courts face doctrinal constraints and are limited to reviewing the federal balance only in the context of “cases and controversies” brought before them.

Accordingly, implementation of a “new federalism” that respects the values of federalism will require conscientious politicians willing to implement a “required considerations” model of federalism. Specifically, federal and state government officials must go beyond the politics and rhetoric of “new federalism” and undertake a fundamental reassessment of how all areas of regulation should be divided between governments applying criteria that focuses on the values that federalism seeks to promote. Indeed, a change in the strategies of governments to the grey areas and yellow zones exposed by globalization might only occur in the context of a overall reassessment. Conscientious politicians at the two levels of government may disagree after weighing the values of federalism. However, the lure of self-interested weighing is reduced if numerous areas of regulation are reassessed simultaneously or at least in succession. The overall reassessment will lead to a reduction in state autonomy with respect to the strategies pursued in response to globalization but also, in all likelihood, to an enhancement of state autonomy in other areas.