NOTES

COMPLIANCE AND MEMBERSHIP VALUE IN INTERNATIONAL ECONOMIC LAW

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ABSTRACT

This Note seeks to present a unified theory of compliance in international economic law. In its first part, it suggests that states and other international actors adhere to international rules and norms because of a set of distinct benefits they obtain by doing so, grouped under the label of membership value. These include, first, the substantive and explicit aims promoted by international agreements, rules, and norms, and, second, a set of ancillary benefits inherent to the activity of international cooperation itself in the forms of reputation, coordination, participation, and global standing. In addition, the Note develops the related concept of system value to explain why global or regional hegemons may sustain multilateral regimes at great direct cost in order to reap the rewards offered by greater international stability and predictability. Furthermore, the Note develops the concept of legal regimes, widening the Note's scope of analysis beyond the traditional notions of law and legal systems to include highly informal and market-based groupings of rules at the international level. In the second part, the Note looks at how legal architecture and enforcement can enhance compliance with these regimes. The Note identifies four means by which this can be achieved: conditionality, risk-weighting, reciprocity, and penalization. The paper then concludes by offering some suggestions of how these means can be employed when designing future international agreements and organizations within international economic law. In particular, it is suggested that financial market access can be leveraged to induce compliance, similar to how markets for goods are used today, and that, overall, participation gains should be used more readily by international organizations to promote compliance.

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I. Introduction

This Note presents a unified theory of compliance within international economic law (IEL) based on assumptions of rational choice. It proceeds in two main parts. In Part II, the Note argues that *obligation*, *membership*, and *system value* are what motivate compliance by international actors with global rules and norms. With an emphasis on the second concept of *membership value*, the Note puts forward and develops a simple thesis: states and other international actors enter into agreements or adhere to international rules and norms because of a set of distinct benefits they attain by doing so. These are, first, the substantive and specific benefits informing the overall objective and purpose of the norms or rules in question, and, second, a set of ancillary benefits in the form of *reputation*, *coordination*, *participation*, and *global standing*. Although most of these benefits have received some attention in academic literature, they have not previously been aggregated and characterized as drivers of compliance within a unified theory. That theory is then contextualized by a discussion of the potential import from the moral obligation international actors may internalize vis-à-vis

international norms and the closely related concept of *system value*. *System value* designates the indirect benefits an actor may receive from maintaining a system at its own expense, in the interest of wider regional or global stability. Recent debates about the value of a rules-based international order have lent increasing importance to a robust understanding of why and how regional and global hegemons benefit from supporting and underpinning the credibility of large, multilateral regimes.

In addition, the Note develops the concept of *legal regimes* to widen its analysis beyond traditional legal systems and international public law to highly informal groupings of standards and criteria recognized by international actors, such as the de facto capital standards used by international banks or the product standards utilized by private manufacturers. By going beyond both formal "hard" and informal "soft" international law to include mere groupings of market-based standards and criteria, this Note is able to present a more comprehensive theory and understanding of the basic incentives underlying norm-building and compliance within the anarchic international system, among a wide range of international actors.

In its second main part, Part III, the Note considers how existing incentive structures can be leveraged to increase compliance through enforcement. On its own, the membership value of a legal regime can induce compliance only to the point where marginal benefit equals marginal compliance cost. However, legal architecture can enhance compliance by designing means through which membership value can be excluded unless certain standards or rules, which the rational actor otherwise would not accept, are met. Such exclusion powers are a core function of legal institutions where enforcement by force and violence is not an option. The Note identifies four means by which an institution can achieve such enforcement and exclusion: *conditionality*, *risk-weighting*, *reciprocity*, and *penalization*. Finally, applying this theory of membership value, enforcement, and exclusion to today's legal organizations, the Note finds that a high degree of enforcement is strongly correlated with high degrees of membership value. On this basis, the Note concludes by offering some suggestions of how legal design can increase compliance by leveraging hitherto overlooked aspects of membership value more effectively.

II. Incentives for Compliance

This part will argue that obligation, membership, and system value constitute the core motivators of compliance with international rules and norms. First, the argument's central thesis is set out, and some of

its underlying theoretical assumptions are examined. This is followed by a brief consideration of the rapid development of the international legal landscape over the last half-century and the emergent and changing definition of "soft law." Finally, the concept of *legal regimes* is introduced. Armed with these conceptual building blocks, the Note then goes on to present the theory of membership value and elaborates on its composition of primary and ancillary benefits. Lastly, before turning to Part III, the related concept of *system value* is briefly discussed.

A. *Theoretical Assumptions*

The Note presents a simple thesis: countries enter into and comply with cooperative arrangements because of the benefit derived from such arrangements, called "membership gains." These gains may differ depending on the values pursued by a state or private actor and the expressed objective of the international agreement. Typical examples of objectives include: environmental protection; the promotion of human rights, rule of law, and democracy; development and economic growth; and combatting terrorism and mutual defense cooperation. As substantive goals, these are referred to as "primary gains" and can be distinguished from the "ancillary gains" inherent to agreement and international coordination itself, such as efficiency, reputation, or agenda-setting/decision-making power. These ancillary benefits are sought regardless of the substantive aims of an agreement and typically do not imply any tradeoffs, such as that between development and environmental protection, or between security and human rights. These labels will be further defined and theorized when the notion of membership value is properly introduced in Section II:D. Before doing so, this section will first further exemplify the notion of primary gains, explore some of the assumptions underlying these labels, and situate them among the multiple academic theories of international relations and law. In particular, this Note does not posit a theory of what ultimately motivates the behavior of states and other international actors. Instead, it posits a theory of what types of benefits international actors may gain from cooperation *regardless* of their ultimate motivations. This Note's core underlying assumption is, therefore, that international actors are rationalistic and motivated by efficiency, whatever their *ultimate* short-, medium-, or long-term goals may be.

The labels designating the abovementioned primary gains are therefore chosen to track actual statements and practice of states and other international actors. With this in mind, it must be recognized that the labels are to an extent arbitrary and born from political process and compromise. The labels can easily be reduced to more fundamental

concepts. To exemplify, the concept of sustainable development has recently emerged thanks to the realization that short-term economic growth at the expense of the environment incurs long-term economic costs. A trade-off between the environment and economic growth is thus in reality a tradeoff between short- and long-term economic benefit. As another example, economic growth may be sought to promote security, which, by the same measure, underlies the primary value of defense cooperation. Indeed, both security and economic gains can be further reduced to vaguer, but more fundamental, concepts, such as state power, independence and sovereignty, or a general notion of utilitarian welfare. The different approaches captured by the primary objectives mentioned above merely represent different means of achieving such ultimate objectives. As a more concrete example, the Paris Agreement on Climate Change's primary objective is to reduce carbon emissions.[1] By adhering, countries gain the primary benefit of reduced carbon emissions. However, for a country like China, the underlying motive to join may be to promote the health of its citizens, which in turn promotes domestic political stability. Yet, because there is no certainty as to what such motives may be, primary benefits designate those aims actually expressed in international legal agreements, which helps the notion of membership benefit track legal practice and avoids controversial arguments of what does or ought to motivate the behavior of international actors.

At the deeper level of inquiry—into ultimate, fundamental objectives—the inquirer no longer seeks to answer the question posed in this Note, namely why international actors comply with international norms. Instead, the inquirer asks what *motivations* underlie compliance and which drive state behavior in general. An inquiry into motivation differs from this Note's central inquiry into what values a state may pursue. The former seeks to determine what those values or interests are, how they are formed, and typically seeks to assess their relative strength in case of conflict, enabling predictions of state behavior. Such predictions have been a central object of international relations and international legal theory. Therefore, although the question of motivation is not the main focus of this Note, before proceeding, it is worthwhile to bring to light the assumptions this Note relies on and situate the present argument within the larger academic landscape.

1. *See, e.g.*, U.N. Framework Convention on Climate Change, *Adoption of the Paris Agreement*, U.N. Doc. FCCC/CP/2015/L.9/Rev.1, arts. 2.1(a), 4.1-2 (Dec. 12, 2015).

There are numerous theories regarding state motivation in international relations, and these are often mirrored in the study of international law. They typically include realism, institutionalism, liberalism, constructivism, the English school, and critical approaches, such as Marxist, feminist, and ecologist theories.[2] Yet, for the purposes of this Note, they can be divided into two camps: instrumentalist theories and norm-based theories.[3] Realism[4] and institutionalism[5] find themselves squarely in the former category, assuming that states act solely in their own self-interest and comply with international law strictly on the basis of a cost-benefit analysis.[6] In contrast, norm-based theories tend to emphasize that state interests are not fixed and unitary, but rather are defined by diverse sets of interests, as well as by beliefs about the nature of the international system and the state's own identity. On this view, a state's actions can be driven by concerns over fairness and legitimacy and not merely its own economic or security interests.[7]

As is often the case, each theoretical perspective contributes important truths to the overall question. In his recent and prominent work on international law compliance from a rational choice perspective, Andrew Guzman identifies as an institutionalist but recognizes the contributions of both constructivism and modern liberalist approaches.[8] Specifically, constructivism may offer explanations of how state interests change over time and how norms such as human rights exercise decisive influence on state behavior.[9] Similarly, liberalism may help explain why international rules look like they do by emphasizing that political leaders and their citizens have divergent interests.[10]

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2. *See* Anne-Marie Slaughter, *International Relations, Principal Theories*, *in* MAX PLANCK ENCYCLOPEDIA OF PUBLIC INTERNATIONAL LAW (R. Wolfrum ed., 2013), http://opil.ouplaw.com/view/10.1093/law:epil/9780199231690/law-9780199231690-e722 (last visited Jan. 10, 2017); *see also* Harold H. Koh, *Why Do Nations Obey International Law Review Essay*, 106 YALE L.J. 2599 (1996).

3. Alexander Thompson, *The Rational Enforcement of International Law: Solving the Sanctioners' Dilemma*, 1 INT'L THEORY 307, 307 (2009).

4. *See, e.g.*, HANS J. MORGENTHAU, POLITICS AMONG NATIONS: THE STRUGGLE FOR POWER AND PEACE (1993); KENNETH N. WALTZ, THEORY OF INTERNATIONAL POLITICS (1979).

5. ROBERT O. KEOHANE, AFTER HEGEMONY: COOPERATION AND DISCORD IN THE WORLD POLITICAL ECONOMY 49-64 (2d ed. 2005) [hereinafter KEOHANE, HEGEMONY].

6. Robert O. Keohane & Lisa L. Martin, *The Promise of Institutionalist Theory*, 20 INT'L SEC. 39 (1995).

7. *See, e.g.*, THOMAS M. FRANCK, FAIRNESS IN INTERNATIONAL LAW AND INSTITUTIONS (1995).

8. ANDREW T. GUZMAN, HOW INTERNATIONAL LAW WORKS: A RATIONAL CHOICE THEORY 20 (2008) [hereinafter GUZMAN, HOW INTERNATIONAL LAW WORKS].

9. *Id.* at 19-20.

10. *Id.* at 20-21.

However, once state interests are understood and fixed, Guzman argues that "rational choice assumptions yield theory that is more parsimonious and predictions that are crisper and more falsifiable than is the case for alternative approaches."[11] In a similar vein, this Note proposes a theory of why states comply with international law based on the rational choice assumption that states and other private actors can recognize their own interests and act in accordance with the benefits and costs of international engagements. Assumptions of rational choice would appear particularly appropriate given the Note's focus on IEL. But as Guzman also notes, a rational choice theory is not bound to consider only behavior that benefits the actor in question. A propensity for other-regarding behavior or to act in accordance with international obligations to the detriment of its own interests can be grafted onto a state's utility curve,[12] meaning the state considers other-regarding behavior to *form part of its own interests*. However, such a move would undermine a rational choice theory's force and degree of falsifiability.[13]

Therefore, for reasons of conceptual clarity and explanatory force, the thesis presented here recognizes the impact that norm-based considerations have on compliance, but chooses to consider norm-based considerations as a distinct type of incentive, different in kind from the direct membership benefit an actor gains when participating in an international arrangement.[14]

As a result, the Note agrees with Abbott et al.'s observation that "obligation" may have an impact on compliance—which is further elaborated upon in the following section—and that both states and other international actors may comply with international law from a sense of duty[15] and because legal rules are considered to be fair and legitimate.[16] However, for the aforementioned reasons, for the most

11. *Id.* at 21.

12. Guzman suggests this approach to capture other-regarding behavior from states at *id.*, at 221 n.3.

13. *Id.* at 21.

14. It should be noted that this approach differs from much of compliance theory, which, as mentioned, has focused on predicting the outcome when these two types of incentives collide, *i.e.*, when negative membership benefit incentivizes an actor to violate its commitments. This Note is thus not interested in the question of which interest prevails in a conflict between norm-based and rationalistic self-interested considerations; it merely notes that if both types of incentives are present, then compliance will follow. Their relative strength or importance is not assessed, although, not unsurprisingly from a cursory glance at the case studies presented below, membership benefit would appear to have the most substantive impact.

15. *See infra* note 85 and accompanying text.

16. FRANCK, *supra* note 7; *see also* Koh, *supra* note 2.

part, the Note will put these considerations aside and focus on the implications and consequences of self-interested behavior.

Before turning to further theorize and explain the notion of membership value in Section II:D, the Note will offer two clarifying sections to underpin the subsequent discussion. First, Section II:B will define the notion of "soft law" and its evolution during the latter half of the past century, which has been characterized by the rise of non-state entities as creators of international norms. Second, Section II:C will clarify that this Note's object of inquiry goes beyond the traditional notions of law and legal systems and encompasses the phenomenon of *legal regimes*. Far from a new concept in and of itself, *legal regimes* merely designate a looser means of grouping and designating sets of rules and norms based on a common social fact, such as a common origin or common objective. However, this concept will be more easily explained if the present state of the international system is first examined, which is what the following section sets out to do.

B. *The New International Landscape*

States have traditionally been the principal international actors and are recognized as such under public international law principles. They are both the subjects and the progenitors of the two main sources of formal international law: treaties and customary international law.[17] Yet, in the 21st century and with the onset of globalization, the international sphere has become increasingly crowded, occupied also by international organizations, corporations, and a plethora of "transnational agency networks" consisting of different regulatory agencies.[18] Many of the international agreements, memorandums, and statements

17. OPPENHEIM'S INTERNATIONAL LAW 24 (Robert Jennings & Arthur Watts, eds., 9th ed. 2008). In addition to those sources of formal international law, the Statute of the International Court of Justice, Article 38(d)-(e), also identifies as sources of international law "general principles of law recognised by civilized nations" and "judicial decisions and the teachings of the most highly qualified publicists of the various nations, as subsidiary means for the determination of rules of law." *Id.*; United Nations, Statute of the International Court of Justice, art. 38, June 26, 1945, 59 Stat. 1031, 3 Bevans 1179, T.S. 993.

18. ANNE-MARIE SLAUGHTER, A NEW WORLD ORDER (2004). Regulatory or government agencies are sub-state bodies staffed by appointed bureaucrats, which may be overseen by ministerial officials, but, when acting as part of transnational networks, do so without direct political direction or sanction. Their international work and its outcomes need not represent official state policy as a whole, but merely the decisions of that agency. International interaction is thus often limited to technical cooperation or information exchanges. As is explained in the preceding as well as the following footnote and accompanying text, this gives rise to a lack of capacity to create international law because these entities are not themselves states, or act on behalf of states as a whole.

concluded within and between such bodies are similar in content and objective to formal treaties, but their authors lack capacity under public international law.[19] In addition, states themselves have increasingly opted to conclude explicitly non-binding agreements.[20] These informal legal agreements, therefore, fail the test of "international law" in the traditional sense, even though their content, object, and purpose bear strong similarities. In modern literature, these agreements have come to be referred to as "soft" law.[21]

Yet, within traditional international legal scholarship, the meaning and nature of soft law has been tied, not to a lack of capacity on the part of its originators, but to its lack of enforceability and compliance. For example, in an influential article, Abbot et al. present a framework for measuring the degree of "legalization," understood "as a particular form of institutionalization characterized by three components: obligation, precision, and delegation."[22] When these three components are maximized, hard legalization follows, while at the opposite end of the spectrum, soft legalization results.[23] First, high levels of "obligation" are achieved when states express consent to be *bound* by the rules agreed, thus implying greater commitment than in the absence of such consent.[24] Second, precision is of importance because "for most rules requiring or prohibiting particular conduct—and in the absence of precise delegation—generality is likely to provide an opportunity for deliberate self-interested interpretation, reducing the impact, or at

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However, both states and private actors may subsequently act in accordance with agency agreements, giving the rules and norms contained therein a "soft" legal character.

19. Thomas Cottier & Lucía Satragno, *The Potential of Law and Legal Methodology in Monetary Affairs*, *in* THE RULE OF LAW IN MONETARY AFFAIRS 411, 417 (Thomas Cottier et al. eds., 2014) (noting that state central bank regulators lack treaty capacity and that their agreements therefore constitute soft law).

20. KERN ALEXANDER ET AL., GLOBAL GOVERNANCE OF FINANCIAL SYSTEMS: THE INTERNATIONAL REGULATION OF SYSTEMIC RISK 138-40 (2006); Kenneth W. Abbott et al., *The Concept of Legalization*, 54 INT'L ORG. 401, 410 (2000). The motivation underlying this trend is discussed in Section II:D *infra*.

21. *See* Joost Pauwelyn in INFORMAL INTERNATIONAL LAWMAKING (Joost Pauwelyn et al. eds., 2012) and by Chris Brummer in CHRIS BRUMMER, SOFT LAW AND THE GLOBAL FINANCIAL SYSTEM: RULE MAKING IN THE 21ST CENTURY (2d ed. 2015) [hereinafter BRUMMER, SOFT LAW] (citing to his two earlier articles Chris Brummer, *Why Soft Law Dominates International Finance—and Not Trade*, 13 J. INT'L ECON. L. 623 (2010) [hereinafter Brummer, *Why Soft Law Dominates*] and Chris Brummer, *How International Financial Law Works (And How It Doesn't)*, 99 GEO. L.J. 257 (2010) [hereinafter Brummer, *International Financial Law*]).

22. Abbott et al., *supra* note 20, at 401.

23. *Id.* at 401-02.

24. *Id.* at 408-12.

least the potential for enforceable impact, on behavior."[25] That is, loosely drafted rules and concepts increase the leeway and opportunities for deviation. Lastly, "delegation" to a third party allows the interpretation and application of rules to take precedence over "political bargaining between parties who can accept or reject proposals without legal justification."[26] Chinkin adopts the same approach as Abbot et al. in suggesting that vague language may render a formal treaty provision "soft" and differentiates between legal and "non-legal" soft law.[27] On these authors' view, soft law is thus associated with low levels of legalization and consequently low levels of enforcement.

In contrast, this Note employs soft law in accordance with its modern meaning: to signify informality and differentiate it from traditional treaty and customary international law. As Abbot et al. themselves point out, definitions should be "broadly consistent with ordinary language,"[28] and because usages have developed, so should our academic definitions. Although controversy remains, soft law is today invoked less after a thorough consideration of an instrument's enforceability, than as an expression of its informality. It has become a convenient shorthand for the plethora of informal international law that has arisen during the latter part of the previous century.[29]

C. *Systems Theory and Legal Regimes*

Thinking of law as a legal *system* has a long pedigree in legal theory. This section will draw on the conclusions of the preceding section and the development toward increased informality within international law to expand the scope of this Note beyond the traditional legal system analysis to a more general rule-and-norms-systems analysis characterized by the notion of legal regimes.

At the heart of law's function lies its ability to create and define the terms of social interaction and cooperation by systematizing, categorizing, and memorializing. To highlight the incentives underlying these processes of social coordination, this Note will go beyond even soft law and take an expansive view of the concept of "law" and the "legal" by extending its analysis to the concept of legal regimes. In international

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25. *Id.* at 413 n.26.

26. *Id.* at 415.

27. C.M. Chinkin, *The Challenge of Soft Law: Development and Change in International Law*, 38 INT'L COMP. L.Q. 850, 851 (1989).

28. Abbott et al., *supra* note 20, at 403.

29. *See, e.g.*, Pauwelyn, *supra* note 21; BRUMMER, SOFT LAW, *supra* note 21; Brummer, *Why Soft Law Dominates*, *supra* note 21; Brummer, *International Financial Law*, *supra* note 21.

relations literature, "international regimes" have been referred to as a set of beliefs and shared expectations, similar to cultural norms.[30] Here, in contrast, "legal regime" is used to refer to a set of rules or standards identified according to a social fact. This social fact could be that they have all been issued by the same authority or that they all relate to or seek to affect the same phenomenon or issue. To exemplify, the International Human Rights Regime would include all international rules on human rights. More narrowly, the United Nations Human Rights Regime would include all rules on human rights promulgated by the U.N. These social facts, such as promulgation by the U.N, are not objective or given a priori. Rather, the definition and existence of a regime depend on which underlying social fact the observer chooses to refer to. This choice of social fact is driven by its utility. For example, an observer may refer to the Global Due Process Regime and posit as the underlying social fact designating this regime's constituent laws and rules *any* laws or rules related to legal due process.[31] However, the concept of such a regime would be of limited utility because the rules would be promulgated by a wide variety of countries, agencies, and legislatures, and the rules would demonstrate great variance and would likely contradict each other. In contrast, the abovementioned U.N. Human Rights Regime, issuing from a single organization and oftentimes shaped by the General Assembly or the U.N. Human Rights Council, would be a much more useful social concept. A radically different, but equally useful, example would be the product standards promulgated by the International Organization for Standardization (ISO).[32] The utility of ISO standards is demonstrated by their widespread use as a point of reference by both states and private commercial actors.

Furthermore, the criteria of a legal regime need not be officially issued, but can be "market-based," meaning that international actors have naturally settled on a set of standards or rules, or behaviors have become sufficiently regular to be categorized as such. For example, whereas the Basel Committee has promulgated capital requirements for banks, there is a different—and higher—standard adopted by

30. KEOHANE, HEGEMONY, *supra* note 5.

31. The choice of label and which social fact is designated as the common denominator shared by the rules and standards of the regime in question is fully within the observer's discretion.

32. Naomi Roht-Ariazza, *'Soft Law' in a 'Hybrid' Organization: The International Organization for Standardization*, *in* COMMITMENT AND COMPLIANCE: THE ROLE OF NON-BINDING NORMS IN THE INTERNATIONAL LEGAL SYSTEM 263 (Dinah Shelton ed., 2000).

market participants.[33] Compliance with a regime, whether intentional or not, is referred to as "membership" in that regime. To join a regime is thus to be in compliance or conformity with its rules and standards. This is not the same as, but includes, official membership in an organization or charter because being a member implies the agent has complied with that organization's membership criteria.[34]

This conception of legal regimes is influenced by H.L.A. Hart, whose positivist legal theory defines law as a system of rules and norms, identified by a common "rule of recognition."[35] By containing the membership criteria of the legal system, the rule of recognition tracks the extent of the system and thereby determines which rules should properly be considered *law*. Consequently, when considering whether a certain rule indeed forms part of the law, the judge will apply the rule of recognition to it. If the rule in question is contained in a properly promulgated statute, the rule of recognition will typically designate it as law. However, if the rule of the recognition contains a doctrine of absurd effects, or if the rule being assessed by the judge breaches a more fundamental constitutional norm, the judge may hold that the statutory rule, despite being validly promulgated, falls outside the scope of the rule of recognition. Importantly, the definition of the rule of recognition itself is constituted by the "practice" of legal officials.[36] Legal officials necessarily recognize and apply an intricate and interrelated web of sources of law, and, therefore, the rule of recognition exists as a matter of social fact. That is, it can be objectively ascertained from the behavior of judges and legal officials.

In comparison to a legal system identified by a rule of recognition, legal regimes are simpler and often less normatively-imbued systems of social rules and standards.[37] The degree of institutionalization is greater

33. *See infra* note 149.

34. Insofar as some actors may ostensibly be members of an organization or a regime, but without honouring their commitments thereunder, this is a problem of enforcement, discussed in Part III. Examples include arrears in membership dues, or countries not living up to agreed budgetary, financial transparency or environmental standards. If, absent enforcement, such failures in commitment are allowed to continue, a divergence will occur between a regime's ostensible standards and its actual, market-based standards, dictated by members' cost-benefit analysis.

35. H.L.A. HART, THE CONCEPT OF LAW 94 (Leslie Green ed., 3d ed. 2012).

36. *Id.* at 110.

37. For a complementary and illuminating application of "complex adaptive system" theory to the emergence of legal "regimes" and "systems" in the context of foreign investment law, see Joost Pauwelyn, *At the Edge of Chaos? Foreign Investment Law as a Complex Adaptive System, How It Emerged and How It Can Be Reformed*, 29 ICSID REV. 372 (2014).

in legal systems, which typically contain clear means for the adjudication and creation of laws.[38] There are, however, important commonalities between legal regimes, soft law, and international law as traditionally understood. By considering not only formal international law, but even mere standards and criteria, this Note is able to present an integrated and coherent theory of the basic economic incentives underlying norm-building in an anarchic system. At the same time, this allows the Note to widen the analysis to the plethora of new multinational actors now active in the sphere of international economic law, painting a more complete picture of the modern international economic system.

D. *Membership Value*

This section returns to the definition of membership value. By joining a legal regime—*i.e.*, by adhering to its rules, norms or standards—the actor gains a range of benefits. Collectively, these benefits constitute the membership value of that legal regime. The greater the regime's membership value, the more likely accession and compliance become.

As already noted, membership value is constituted by a set of primary or substantive benefits, which inform the reason for adherence to international rules. These are linked to the main purpose underlying the regime, such as increasing economic growth, reducing systemic risk, or promoting human rights. Because this Note confines itself to the field of IEL, it will mainly consider the primary benefits of the two former categories, alongside benefits such as increased trade and investment. Yet the theory is more widely applicable, and other areas of international law will be referred to where appropriate.

In addition, regardless of a regime's overall objective, a set of ancillary gains will accrue to the agent by virtue of the act of compliance itself, in the form of reputation, participation, global standing, and coordination. This section will examine each of these in turn.

1. Coordination Gains

Coordination gains are understood as the efficiency gains arising from cooperation and agreement on common standards within a

38. Hart considers that, in addition to the more general rule of recognition, a legal system will also contain "rules of change" and "rules of adjudication," designating how these processes are conducted within the system. *See* HART, *supra* note 35, at 94-96.

regime of more than two actors; they tend to be one of the most well-recognized benefits of legal agreements.[39] Even within traditional legal theory, the ability of law to privilege a certain social convention through its coordinative function, and thereby create moral reasons for action in accordance with that convention, is well-recognized.[40]

Unlike the other ancillary benefits, coordination may even represent the central objective of many agreements. The technical product standards produced by the ISO are a case in point.[41] Their objective is to coordinate and thereby facilitate trade and production of goods thanks to a common frame of reference. In this context, coordination is no longer an ancillary benefit, but the main objective of the organization and its agreements. Such standardization represents de jure standardization. Standardization can also arise de facto, where the community responds to the practice or specifications of an early mover.[42] Interestingly, empirical work by Farrel and Saloner demonstrates that de jure coordination appears to provide greater efficiency gains than that produced by the network effects from de facto market-driven coordination.[43] This illustrates not only the value of coordination through legal process but also the value of law itself as a tool for social ordering: by suggesting certain standards, these become initial points of reference and create a gravitational pull for actors around which to order their behavior.

2. Reputational Gains

Reputation for compliance has long been recognized as a key incentive for states to comply with international law.[44] Guzman considers it to be the most important incentive, superior to both the threat of

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39. *See, e.g.*, ABRAM CHAYES & ANTONIA HANDLER CHAYES, THE NEW SOVEREIGNTY: COMPLIANCE WITH INTERNATIONAL REGULATORY AGREEMENTS 4 (1995) (referring to "efficiency" of agreements); GUZMAN, HOW INTERNATIONAL LAW WORKS, *supra* note 8, at 26-27.

40. *See generally* E. LAGERSPETZ, THE OPPOSITE MIRRORS: AN ESSAY ON THE CONVENTIONALIST THEORY OF INSTITUTIONS (1995). For a critique, see Leslie Green, *Positivism and Conventionalism*, 12 CAN. J.L. & JURIS. 35 (1999).

41. Roht-Ariazza, *supra* note 32, at 263-65.

42. Paul Wakke et al., *The Relationship between Innovation in Services and Standardization: Empirical Evidence of Service Providers' Involvement in Standardization* (Apr. 26, 2012), http://ssrn.com/abstract=2045484 (last visited Jan. 9, 2017).

43. Joseph Farrell & Garth Saloner, *Coordination Through Committees and Markets*, 19 RAND J. ECON. 235 (1988).

44. Robert Keohane has been one of the earlier and most prominent proponents of the concept in international relations scholarship. *See* KEOHANE, HEGEMONY, *supra* note 5; *see also* Brummer, *International Financial Law, supra* note 21, at 284-86.

retaliation and the reciprocal suspension of benefits.[45] Following the literature, Guzman defines reputation as "judgments about an actor's past behavior used to predict future behavior."[46] His core argument is that international interactions can be characterized as a series of iterative games, where reputation operates as a signaling mechanism allowing for credible commitments into the future.[47] If previous violations have drained an agent's reputational capital, other international actors are unlikely to agree to renewed cooperation in the future.[48]

Even critics of a reputation-based approach tend to concede that reputation for compliance has some impact on a state's willingness to comply with international law.[49] It is, however, important to point out that reputation for compliance in one area of the law may not carry over into another and that states may value not only a reputation for compliance, but also a reputation for *non-compliance* with international law.[50] For example, a state may wish to signal that it will ignore its human rights obligations to maintain domestic stability. In addition, it is unclear whether, how, or to what extent reputation attaches to the state itself or merely the government of the day. This may drastically alter time horizons and the extent to which the state as a whole internalizes any reputational gains and losses. Finally, due to the expansive nature of the concept of reputation, it can also be hard to find empirical evidence of the extent of its impact.[51] However, on several of these points, IEL proves an interesting exception. As the following examples will show, numerical values are often readily available, and the commercial nature of IEL lends itself well to the calculability and rational actor presumptions underlying a reputational analy-

45. GUZMAN, HOW INTERNATIONAL LAW WORKS, *supra* note 8.

46. *Id.* at 33 (citing Gregory D. Miller, *Hypotheses on Reputation: Alliance Choices and the Shadow of the Past*, 12 SECURITIES STUD. 40, 42 (2003)).

47. GUZMAN, HOW INTERNATIONAL LAW WORKS, *supra* note 8, at 34-41, 74-77. The anarchical system presents states with a prisoner's dilemma. Whereas cooperation brings efficiency benefits, all states face high individual incentives to defect, even though a defection by a majority is likely to make everyone worse off. If states can signal their own commitment, other states are less likely to defect themselves and will be more inclined to enter cooperative arrangements in the first place. *See also* KEOHANE, HEGEMONY, *supra* note 5, at 75.

48. BRUMMER, SOFT LAW, *supra* note 21, at 145.

49. *See* Rachel Brewster, *Unpacking the State's Reputation*, 50 HARV. INT'L L.J. 231, 269 (2009).

50. *Id.* at 238, 246, 259-66; Robert O. Keohane, *International Relations and International Law: Two Optics*, 38 HARV. INT'L L.J. 487, 501 (1997).

51. One of Brewster's main critiques is that reputation is treated as an "error term," *i.e.*, its lack of falsifiability allows it to be used too flexibly to explain any kind of behavior. *See* Brewster, *supra* note 49, at 269.

sis. In addition, there is evidence that actors operating within IEL—be they states or public or private bodies—attach reputations to governments, rather than to other states as a whole, and that rule-adherence is indeed accounted for when decisions are made whether to trade or invest.

Turning first to the topic of sovereign debt, Michael Tomz's *Reputation and International Cooperation* offers an intriguing and expertly argued reputation-based theory, backed up by empirical studies.[52] Based on what are detailed records of past debt repayments and the economic conditions prevailing at the time, the author argues that states obtain reputations in the eyes of private investors as "stalwarts, fair-weathers, and lemons."[53] If state behavior defies its reputed archetype, investors will adjust their beliefs "by taking a weighted average of old and new evidence."[54] Therefore, in contrast to other, similar reputation-based theories, Tomz does not presume that investors operate under conditions of complete information.[55] Tomz presumes, furthermore, that private investors attach reputations to governments and not states, taking account of political stability and domestic political pressures over relatively short time periods.[56] Consistent with these assumptions, Tomz finds that due to a lack of historical data, investors applied a reputational discount to new entrants to state capital markets in the 18th and 19th century, at a time when many new states were formed.[57] Behavior and records of bankers, analysts, fund managers,

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52. MICHAEL TOMZ, REPUTATION AND INTERNATIONAL COOPERATION: SOVEREIGN DEBT ACROSS THREE CENTURIES (2007).

53. *Id.* at 17 (emphasis omitted).

54. *Id.* at 18-20.

55. *Id.* at 15.

56. *Id.* at 20-23. As a typical example, Tomz cites the Argentine debt saga, where voters in the country's 1999 election initially rejected candidate Duhalde, who suggested a suspension of debt payments to international private creditors. *Id.* at 12. However, domestic opinion shifted in favor of default, and, after devastating results in the 2001 congressional elections and amid civil unrest, his rival, Fernando de la Rúa, was forced to resign. His successor immediately declared sovereign default. *Id.* However, a few holdout investors refused to settle their claims and eventually managed to block Argentine access to capital markets via suits in U.S. courts. Creditor opposition continued under Presidents Néstor and Christina Fernández de Kirchner, but by supporting the repayment of creditors, Maurici Macri was able to win the presidency in 2015, and to reach a settlement in 2016. Benedict Mander & Elaine Moore, *Argentina puts an end to long holdouts saga*, FT (Apr. 22, 2016), https://www.ft.com/content/516ab98a-08a1-11e6-876d-b823056b209b?mhq5j=e7. As this example highlights, government reputations and intentions are more relevant than that of the country over time, even though past political precedent may have some impact on how governments behave.

57. TOMZ, *supra* note 52, at 39-69.

and rating agencies from the 1920s and 1990s reinforce the conclusion that state reputation matters to investment decisions, and far more than the availability of trade sanctions as a tool for enforcement.[58]

In theory, the same applies to international investment, although the empirical evidence on whether state accession to bilateral investment treaties (BITs) has increased foreign direct investment (FDI) is mixed.[59] It can of course be suggested that even if FDI volumes have not clearly increased, they might otherwise have decreased. Or, consistent with the reputational assumptions presented in this section, merely signing a BIT may not generate reputational gains; there must also be adherence over time. However, in what could be described as a catch-twenty-two situation, investment is needed before such adherence can take place.

In contrast, another major pillar of IEL, trade policy, is different from both lending and FDI for a number of reasons. First and foremost, trade policy is negotiated and arbitrated between states. Second, and in part as a consequence of this, there are fewer sunk costs exposed to capture by a recalcitrant state.[60] If quotas or tariffs are imposed, the foreign producer will simply cease exports and look for other markets. And even though an exporter may face some loss from prior investments in advertising or supply networks or through disruptions of multinational supply chains, these issues fall closer to investment law than trade. Third, it is more likely that trade is reciprocal, meaning that other states can retaliate by imposing their own border measures, and, in the past two decades, this process has been mediated by the World Trade Organization's (WTO) Dispute Settlement Body. Exporters are, therefore, less reliant on reputation when choosing where to export, although it has been argued that countries nevertheless still consider reputations for compliance important.[61]

Unfortunately, an in-depth assessment of these and other areas of IEL is beyond the scope of this paper, yet the above examples sufficiently illustrate the point sought to be made.[62] As already mentioned

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58. *Id.* at 70-85.

59. Peter Egger & Michael Pfaffermayr, *The Impact of Bilateral Investment Treaties on Foreign Direct Investment*, *in* THE EFFECT OF TREATIES ON FOREIGN DIRECT INVESTMENT 253 (Karl P. Sauvant & Lisa E. Sachs eds., 2009).

60. Andrew T. Guzman, *Why LDCs Sign Treaties That Hurt Them: Explaining the Popularity of Bilateral Investment Treaties*, 38 VA. J. INT'L L. 639, 664-65 (1997).

61. *See* Matthew C. Turk, *Why Does the Complainant Always Win at the WTO?: A Reputation-Based Theory of Litigation at the World Trade Organization*, 31 NW. J. INT'L L. & BUS. 385 (2011).

62. For example, government procurement or arms contracts directly negotiated between sovereigns. How reputation affects commercial transactions between states and private companies has received comparably scarce attention in the empirical literature, although it is clear that a

and highlighted by these examples, compliance with IEL lends itself particularly well to a reputation-based analysis because the behavior of economic actors is closely aligned with the assumptions of rationality and calculability of costs and benefits due to its commercial nature. Moreover, the same assumptions apply both to state and non-state actors operating at the international level—for example, multinational corporations and banks. Inclusion of these actors allows for richer comparisons and a more nuanced view of international law. Some of the above criticisms against reputation, therefore, find less of a foothold within the context of IEL.

Reputation may matter less in other areas of international relations compared to IEL. As Brewster highlights, for international agreements designed to foster public goods, the reputational impact may be negligible.[63] Climate change is a good example. Canada defaulted on its legal commitments under the first commitment period of the Kyoto Protocol (2008–2012), and to avoid the sanctions that would have applied during the second commitment period (2012–2020), Canada abstained from participating (as did Japan and Russia).[64] However, this did not disadvantage or preclude its membership in the Paris Agreement, concluded in 2015 as the successor to the Protocol,[65] although one may speculate that Canada exercised less influence during the negotiations. By necessity, the Paris Agreement was envisaged as a "universal global accord," and this collective action problem inherent in public goods cooperation will be further discussed in Section III:F below.

3. Comparison Between Reputation and Primary Gains

Before moving on to consider global standing, a point of clarification is in order. Reputational gain is not to be confused with the aforemen-

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national, origin-based reputation for quality affects consumer's purchasing habits from private producers in that country. *See* Rodney E. Falvey, *Trade, Quality Reputations and Commercial Policy*, 30 INT'L ECON. REV. 607, 609-13 (1989).

63. Brewster, *supra* note 49, at 245.

64. *Canada pulls out of Kyoto Protocol*, THE GUARDIAN (Dec. 13, 2011), https://www.theguardian.com/environment/2011/dec/13/canada-pulls-out-kyoto-protocol.

65. The United States, who signed but never ratified the Kyoto Protocol, also did not appear to suffer from its previous non-participation. However, this may in part be due to a change in administrations, highlighting the point made earlier that reputation attaches to governments—and the U.S. Congress certainly gained a reputation for climate change opposition. Such was not the case in Canada, however, where the liberal Prime Minister Justin Trudeau took over from conservative Stephen Harper, who had overseen the Kyoto exit three years earlier, only a few weeks prior to conclusion of the Paris negotiations.

tioned primary gains of membership. Primary gains accrue from the nature of the regime itself. They may accrue at the moment of accession and then remain constant. Conversely, reputational benefits accrue *only* over time and accrue, not from the nature of the regime, but from the act of compliance itself. Recalling the definition above, an actor's reputational capital is fundamentally a risk profile based on others' beliefs about its future behavior.

To exemplify, an investor may agree to extend a loan if a borrower complies with a set of criteria. The primary gain from compliance is, thus, the loan. However, if the borrower has a low reputation for compliance or no history by which to assess it, the lender may increase the interest rate, increase the security demanded, or even decrease the amount of the loan. As the borrower increases her reputation by complying over time, these harsh terms may be renegotiated. The same would be true for a firm that commits itself to a stricter disclosure regime by cross-listing its shares on a foreign stock exchange with more robust monitoring requirements[66] or by adopting global accounting standards. Its gain from compliance would be that some investors who previously would not have considered buying the stock would decide to do so. As the firm builds its reputation for compliance by remaining a member of the foreign exchange or by continuing to abide by global accounting standards, investors will eventually increase their holdings as their perception of risk decreases.

This is the reason international actors value reputational gains. In complex regimes, a baseline of reputation is usually needed to secure any substantive membership benefit whatsoever. Like the point made earlier, if a country with a reputation for expropriating foreign investment concludes a BIT, this accession to an international regime may not yield the expected benefit if the state is unable to prove that it will continue to adhere over time. However, in simple, pure coordination agreements, a reputation for compliance is not relevant. A country deciding to switch from driving on one side of the road to the one its neighbors use will instantly reap the coordinative benefits, and those benefits will remain constant for as long as compliance is maintained. At this extreme, compliance and the consequent membership benefits are binary (coordinated or uncoordinated approach), whereas, at the other extreme, as in the BIT example, primary benefits may be wholly dependent on high reputation.

66. BRUMMER, SOFT LAW, *supra* note 21, at 137, 148-49.

4. Global Standing

Brewster makes an often overlooked but crucial distinction between "global standing" and "reputation for compliance."[67] The latter concept is what has been discussed so far. By complying, an international actor accumulates reputational capital. This allows the actor to enter similar arrangements on good terms in the future. Reputational capital is spent—sometimes altogether—in case of a violation.

In contrast, global standing, or "global public opinion," is connected to a country's popular perception.[68] It may be considered a species of "soft power"[69] and is thus certainly a benefit attained from adherence to international norms. However, reputation for compliance and global standing can at times be mutually exclusive. As Brewster points out, a refusal to join agreements or to take on onerous obligations by adopting treaty reservations may be a way to ensure a reputation for compliance, but will inevitably hurt a country's global standing.[70] Furthermore, Brewster remarks that "violations of international law might *improve* the popular perception of the state with a global audience" and cites the North Atlantic Treaty Organization (NATO) bombing of Serbia to forestall further ethnic cleansing in the 1990s.[71]

Global standing is thus a looser concept operating across issue areas and is, therefore, also more difficult to directly leverage for primary benefit. It represents an aggregate of people's perceptions of a country as being a positive and constructive force for good—generally boosted by international law compliance, but easily undermined even by temporary or highly publicized missteps. Reputation on the other hand, as already remarked, operates in closed silos. A state's credit score will not be affected by non-compliance with its human rights or environmental obligations, insofar as this does not contribute to political instability. As also remarked, a reputation for ignoring such concerns could even be thought to bolster creditor confidence. Any reticence by another state, investor, or company to deal with a country of unscrupulous repute can in fact be more closely explained by moral considerations of fairness, than international reputation as typically understood. Indeed, applying

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67. Brewster, *supra* note 49, at 238.

68. *Id.*

69. *See generally* JOSEPH S. NYE, SOFT POWER: THE MEANS TO SUCCESS IN WORLD POLITICS (2005).

70. Brewster, *supra* note 49, at 238-41.

71. *Id.* at 240. Absent U.N. Security Council authorization, it is difficult to argue that the military intervention was permitted under international law. However, at least in some countries, the intervention had considerable support on humanitarian grounds. It would thus have contributed to the participants' global standing in those countries.

such considerations of fairness to its dealings would be a means for a state to boost its global standing. Global standing could thus as easily be labelled "moral standing." Given these clear differences between the concepts of reputation and global standing, it is important to avoid conflating them.[72]

Finally, it should be noted that a low global standing or a low reputation for compliance is likely to directly impact an actor's ability to negotiate and influence others. However, instead of treating influence as a mere byproduct of reputation and global standing, this Note looks at influence as a separate and more complex membership benefit under the label of "participation gains." This concept is explored in the next section, as the fourth and final ancillary benefit contained under the umbrella of membership value.

5. Participation Gains

As in any group setting, compliance with group norms allows the agent to more easily take leadership, influence the direction of a given group, and convince others to also comply with its rules.[73] Participation gains thus refer to the influence a member may obtain over the agenda, contents, and other members of a regime the agent has joined.

Participation gains arise within both unstructured and organizationally-sophisticated regimes. Yet, in many of the latter types of legal regimes, the members of the regime are not the same as those promulgating it. For example, it is not the securities firms themselves but government officials who sit on the board of the U.S. Securities and Exchange Commission and write its rules. For such regimes, membership in the regime—*i.e.*, compliance with its rules or standards—does not grant an ability to influence its contents, and thus participation gains are precluded.[74] However, in self-regulatory organizations, such as the Basel Committee, where the state central bank regulators write the rules they then undertake to implement domestically, or, in the case of many professional bodies in domestic legal systems, membership can often be dependent on compliance.[75] This can even be the case in democratic legal systems. In the United Kingdom, imprisoned offend-

72. For a recent example where this distinction is not clearly made and where the cogency of the analysis is unfortunately undermined, see JENNIFER L. ERICKSON, DANGEROUS TRADE: ARMS EXPORTS, HUMAN RIGHTS, AND INTERNATIONAL REPUTATION (2015) (arguing that "social reputation" can explain why states have chosen to enter into international arms trade treaties).

73. BRUMMER, SOFT LAW, *supra* note 21, at 145.

74. This is ignoring any moral or expertise-based claim the regulated entities may have.

75. *See infra* Section III:C.

ers lose their right to vote.[76] In these cases, compliance, therefore, yields enhanced institutional standing and influence over the contents and continued development of the regime.

Among states and state regulators, self-regulation is the rule and not the exception.[77] As an illustrative example, the Articles of Agreement of the International Monetary Fund (IMF) allows for the suspension of voting rights in the case of non-compliance.[78] Similarly, a central argument in the Brexit debate on the United Kingdom's exit from the European Union (EU) was that the United Kingdom would be able to continue to influence the content of EU rules should it remain a member. Incidentally, the Obama administration used the same argument when promoting the Trans-Pacific Partnership (TPP) by emphasizing how its own participation would take away influence from China.[79] Although participation value is highly dependent on the structure of the regime in question, there is little doubt that states and other actors will give it due consideration where circumstances allow.

E. *System Value*

For the sake of completeness, this Note also introduces the supplemental notion of "system value." This is a much more limited concept than membership value and represents the indirect gain a state may obtain from the *existence* of a legal regime. Importantly, membership value does not go beyond a state's direct benefit from compliance and participation. However, certain states may be interested in setting up regimes, which, by helping other nations, engender regional stability and positive spillover effects. This is not charity because the state is still self-interested.

How system value expresses itself in practice is best explained by looking at a few illustrative examples. A first such example is the IMF

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76. Representation of the People Act 1983, c.2, § 3 (Eng.), http://www.legislation.gov.uk/ukpga/1983/2. Although in Hirst v. The United Kingdom (No. 2), 2005-IX Eur. Ct. H.R. 187, 220, the European Court of Human Rights ruled this incompatible with Protocol 1, Article 3 of the European Convention on Human Rights, sparking an on-going row with the British government.

77. Examples of self-regulatory bodies of state regulators include, among others, the International Accounting Standards Board (IASB), International Organisation of Securities Commissions (IOSCO), and the International Association of Insurance Supervisors (IAIS).

78. Articles of Agreement of the IMF, art. 15, § 2(b), Dec. 27, 1945, 60 Stat. 1401, 2 U.N.T.S. 39.

79. Barack Obama, Editorial, *America, Not China, Should Call the Shots on Trade*, WASH. POST, May 3, 2016, at A15.

loan quotas that states are entitled to draw on in times of need.[80] For the United States, the world's largest economy both in 1945 and now, those quotas are a liability and not a benefit. Yet the United States had and continues to have an acute interest in the stability of the global economy, which is why such a system of guaranteed borrowing at low interest rates is valuable to maintain.

A similar example is the Chiang Mai Initiative Multilateralization, which is an agreement among ASEAN members together with Japan, China, and South Korea. It provides swap lines to members in need as between their central banks, up to a combined value of $120 billion.[81] Countries like China and Japan do not derive direct benefits from the regime, but staving off financial crises among their neighboring economies still yields indirect benefits.

Another obvious example is NATO. Although U.S. military spending is much higher than that of its allies, the stability the alliance promoted after the Second World War has long been seen to be in the U.S. interest. After the war, Germany's and Japan's low military spending was welcomed, and mutually reinforcing arms-races were avoided. Indeed, NATO is a clear illustration of how system value can be characterized as an expression of the gains derived from avoiding a prisoner's dilemma.[82] Where a global or regional hegemon is able to commit credibly and underpin a system of institutional norms, other countries will be able to rely on those norms without fearing that others will defect at their expense. It was this reasoning that was the basis of the alarm expressed by policy makers when the Trump administration refused to voice its clear support for the mutual defense guarantee contained in Article 5 of the NATO treaty.[83] Therefore, even though President Trump's distinct foreign policy is often described as "transactional" and as promoting U.S. self-interest,[84] an under-appreciation of system value means overlooking how even self-interested actors have

80. On the function and history of the IMF, see generally Andreas F. Lowenfeld, *The International Monetary System: A Look Back Over Seven Decades*, 13 J. INT'L ECON. L. 575 (2010).

81. CHRIS BRUMMER, MINILATERALISM: HOW TRADE ALLIANCES, SOFT LAW AND FINANCIAL ENGINEERING ARE REDEFINING ECONOMIC STATECRAFT 147 (2014).

82. Explained further in note 47 *supra*.

83. Arthur Beesley et al., *Donald Trump Fails to Endorse NATO's Mutual Defence Pledge,* FT (May 25, 2017), https://www.ft.com/content/9212b3ea-416a-11e7-82b6-896b95f30f58. President Trump eventually did endorse Article 5 in a speech in June that year. *After sowing doubts, Trump backs NATO mutual defense under charter*, REUTERS (Jun. 9, 2017), https://www.reuters.com/article/us-usa-trump-nato/after-sowing-doubts-trump-backs-nato-mutual-defense-under-charter-idUSKBN1902U9.

84. *See, e.g.*, Stewart M. Patrick, *Trump and World Order,* FOREIGN AFF. (Apr. 2017), https://www.foreignaffairs.com/articles/world/2017-02-13/trump-and-world-order.

reasons to support multilateral systems and institutions. Although the hegemon has to expend direct costs in maintaining such systems, it reaps the indirect benefits of peace and prosperity by promoting stability and predictability.

System value thereby represents a third type of incentive alongside obligation and membership value. Like the latter, its underlying motivation is the agent's self-interest.

III. Legal Enhancement and Architecture

Part II argued that obligation, membership, and system value motivate compliance with legal regimes. This part looks at how legal architecture and engineering can enhance these incentives and at membership value in particular.

The approach taken bears similarity to that of Abram and Antonia Chayes. In their influential book *The New Sovereignty*, the authors identify "efficiency," "interests," and "norms" as the reasons why states have a natural propensity to comply with international law.[85] Although rendered with less complexity, their factors correspond to many of the factors identified in this paper. The idea of obligation presented here is similar to the authors' idea of norms, by which compliance is motivated by "a general sense of duty."[86] Likewise, "interests" signify the fact that states carefully negotiate international commitments in accordance with their preferences[87] and thus bear similarities to what is here recast as substantive benefit: the idea that states enter into agreements in order to obtain specific, sought-after benefits. Finally, the Chayeses' notion of efficiency is equivalent to coordination gains.[88]

On the basis of these three characteristics, the authors assume that states share a general propensity to comply with international obligations[89] and argue that, apart from certain highly egregious cases, most defections of international law are unintentional.[90] The authors identify three main causes for this non-compliance: "ambiguity and indeterminacy of treaty language," "limitations on the capacity of parties to carry out their undertakings," and "the temporal dimension of the social, economic, and political changes contemplated by regulatory

85. Chayes & Chayes, *supra* note 39, at 3-9.
86. *Id.* at 8, 306 n.24.
87. *Id.* at 4-7.
88. *See supra* note 39 and accompanying text.
89. Chayes & Chayes, *supra* note 39, at 3.
90. *Id.* at 9-10.

treaties," *i.e.*, unanticipated developments.[91] The authors then go on to develop their model of "regime management," as opposed to the standard "enforcement model," to seek to overcome these causes.[92]

This Note draws from the authors' rich contributions, agrees with many of their insights, and likewise identifies a set of reasons for compliance. But, instead of seeking to overcome causes of non-compliance, it presents suggestions for how compliance can be enhanced. The Note, therefore, presents a complementary account, with a clear focus on enforcement. To this end, the next section, III:A, offers a definition of enforcement, followed in III:B by an examination of the means by which enforcement can be achieved. Section III:C then discusses which types of benefits are most amenable to enforcement, and Section III:D emphasizes reporting and monitoring as important prerequisites to effective enforcement. In Section III:E, the Note makes brief mention of some further considerations which deserve mention, but fall outside the scope of the present inquiry. Finally, in Section III:F, the implications arising from the above findings are discussed, and the Note observes that high degrees of membership value correlate strongly with high degrees of compliance and enforcement.

A. *Enforcement: Hard and Soft Law*

Enforcement occurs where a rule is upheld and/or applied in the face of uncertainty or ambiguity, or where a defection from a rule is met by a sanction, "defined as the withholding of a benefit or the imposition of a penalty."[93] To an extent, enforceability may depend on the nature of the rule or legal obligation sought to be enforced. When states decide to take legal action, they can choose to do so via formal (hard) or informal (soft) law. The reasons why a state may opt for the latter has been well documented. Soft law allows for greater flexibility and ease of negotiation, lower sovereignty costs by representing less delegation to interpretive bodies, and may facilitate compromise more easily.[94] However, the impact of formalization is often exaggerated. It is not the case that soft law precludes enforcement, or that hard law is a prerequisite for enforcement. Such a presumption finds greater sup-

91. *Id.* at 10.

92. *Id.* at 3, 10, 109-285.

93. ALEXANDER ET AL., *supra* note 20, at 141.

94. Kenneth W. Abbott & Duncan Snidal, *Hard and Soft Law in International Governance*, 54 INT'L ORG. 421 (2000); Brummer, *Why Soft Law Dominates*, *supra* note 21, at 630-34; Ellis Ferran & Kern Alexander, *Can Soft Law Bodies Be Effective? The Special Case of the European Systemic Risk Board*, 35 EUR. L. REV. 751, 756 (2010).

port in the domestic legal setting, where the legal system grants a general power to members to have their claims adjudicated by the court system, which is then backed by the state's monopoly of violence. Yet courts are not the only means by which law can be enforced. A range of reputational and market-based mechanisms constantly operate to enforce compliance by imposing negative consequences on deviant actors, and those mechanisms are of special importance in the international context. As Chris Brummer explains:

> Plenty of hard law, treaty-backed regimes are not especially durable. UN resolutions concerning human rights and the environment are often ignored, just as commitments under trade regimes can be suspended, especially in times of economic stress. Moreover . . . soft law can have its own hard edges. Reputational costs arising from backtracking or ignoring international regulatory standards can be high, even when agreements are informal.[95]

These enforcement mechanisms will be further explored in the following sections. The Note will demonstrate how the essence of enforcement in international law does not depend as much on the formal/informal dichotomy[96] as on the exclusion of membership value. There is no inherent reason why such enforcement is not equally applicable to both hard and soft law.

B. *Exclusion Powers*

Section II:D argued that membership value constitutes one of the chief reasons why states and other international actors comply with legal regimes. The ability to increase compliance, therefore, depends on the ability to exclude such benefits from the defector's enjoyment as soon as defection becomes apparent, or to make those benefits conditional on compliance ab initio. This section considers four means, or legal *exclusion powers*, by which this is achieved within the international legal system: *conditionality*, *risk-weighting*, *reciprocity*, and *penalization*. Most of the ancillary benefits inherent to compliance are automatically forfeit: namely reputation, global standing, and (in most cases) coordination gains. In contrast, the loss of participation and primary benefits

95. BRUMMER, SOFT LAW, *supra* note 21, at 179.
96. *Id.*

typically depends on the structure of the legal regime, as well as the motivation of its other members.

The *types* of benefits excluded, as opposed to their means of exclusion, are subsequently discussed in Section III:C, followed by a brief consideration of publicity and monitoring as a necessary prerequisite to successful enforcement.

1. Positive Conditionality

In the literature, conditionality usually refers to the conditions under which the IMF and World Bank lend money to countries facing a balance-of-payment crisis.[97] Among the countries that have had recourse to such loans, conditionality has been an effective instrument in incentivizing compliance with a range of international standards and best practices, otherwise monitored under the IMF and World Bank's Financial Sector Assessment Program (FSAP), such as the Basel Accords, insurance, securities, and other financial market standards, as well as privatization and recapitalization standards.[98] Yet the program is limited by the fact that rich countries are not in need of aid escape monitoring and that, even where loans are staggered to ensure that the required standards are continually implemented, the IMF and World Bank have often been reluctant to pause disbursements.[99]

Although the IMF/World Bank conditionality is an illustrative example, this Note uses conditionality in its wider sense to refer to any kind of benefit granted or withdrawn subject to conditions. A normal bank loan would, therefore, also be classed as conditionality-based. Another highly typical example is the Generalized System of Preferences (GSP) within the WTO regime, whereby developed countries may grant special tariff concessions to select developing countries, subject to certain conditions. These may include a wide range of good governance and human rights standards.[100]

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97. *Id.* at 152-54; ALEXANDER ET AL., *supra* note 20, at 144-45.

98. BRUMMER, SOFT LAW, *supra* note 21, at 95-96, 152-53; *see* ALEXANDER ET AL., *supra* note 20, at 144-45.

99. BRUMMER, SOFT LAW, *supra* note 21, at 153-54.

100. *See, e.g.*, European Commission, *Generalised Scheme of Preferences (GSP),* http://ec.europa.eu/trade/policy/countries-and-regions/development/generalised-scheme-of-preferences/ (last visited Jan. 9, 2017).

2. Negative Conditionality

Negative conditionality is merely the reverse of the aforementioned positive variant. The difference is that it operates to withdraw or suspend an *existing* benefit until specified conditions are met and, like all sanctions and enforcement actions, it operates in response to a violation. An example would be economic sanctions imposed over the Iranian or North Korean nuclear programs—with the expectation that sanctions will be lifted if compliance is attained.

3. Risk-weighting

Risk-weighting recalls previous discussions in Section II:D(2) on the effects of lost reputational capital in case of non-compliance and refers to the increase in risk premium imposed on a defector subsequent to breach. Risk-weighting will often work in tandem with conditionality. For example, normally, certain minimum requirements will have to be met by each party before they are willing to transact or negotiate. These minimum requirements may simply reflect commercial prudence, such as demands for minimum capital buffers or that the counterparty take out insurance, or they may be imposed on moral grounds, like human rights standards.[101] Yet beyond these absolute requirements, the counterparties to any agreement will use risk-weighting to manage interest rates, collateral, ancillary guarantees, advances on performance, risk-allocation, gestures of goodwill, etc.

There may be objection to labeling risk-weighting as a means of enforcement because it merely represents a realignment of costs and benefits when new information about the defector is priced and internalized. However, failing to recognize this behavior as proper enforcement would overlook the potent capacity of market forces to suspend benefits to defectors even in the complete absence of a central regulating authority.

4. Reciprocity

Reciprocity is a term of art in international law and is set out in Article 60 of the Vienna Convention on the Law of Treaties: "[a] material breach of a bilateral treaty by one of the parties entitles the

101. An example is the labor and environmental provisions included in the "overall trade negotiation objectives" of the latest U.S. Trade Promotion Authority legislation. *See* Section 2 of the Bipartisan Congressional Trade Priorities and Accountability Act of 2015, S. 995, 114th Cong. § 2 (2015).

other to invoke the breach as a ground for terminating the treaty or suspending its operation in whole or in part."[102] Reciprocity thus resets the relationship between the parties and denies the defector any further primary or ancillary benefits. The concept will be used here to signify situations where the parties to the regime have similar mutual obligations, although this need not be the case in international law generally.

As Guzman remarks, reciprocity is the most effective in bilateral relationships,[103] but the WTO is a good example of an effective multilateral regime founded largely on reciprocity. A defection from the General Agreement on Tariffs and Trade (GATT) gives the offended party a right to retaliate by suspending its tariff concessions and the market access granted to the offender, unless or until the latter withdraws the offending measure.[104] As a rule, retaliation is compensatory,[105] in line with the logic of reciprocity in a situation of mutually equivalent obligations.

An area outside the formal treaty context where reciprocity has come to the fore is in international banking and securities regulation between the EU and the United States. Whereas the two jurisdictions have in the past sought to operate systems of "substituted compliance" by recognizing the surveillance of the other national regulators as sufficient,[106] after the Financial Crisis, the development has been toward further fragmentation. In response to rules published by the U.S. Federal Reserve in 2014, requiring foreign bank subsidiaries operating

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102. Vienna Convention on the Law of Treaties, May 23, 1969, art. 60, 1155 U.N.T.S. 331, 8 I.L.M. 679 (entered into force Jan. 27, 1980).

103. GUZMAN, HOW INTERNATIONAL LAW WORKS, *supra* note 8, at 42.

104. General Agreement on Tariffs and Trade art. XXIII, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1A, 1867 U.N.T.S. 187, 33 I.L.M. 1153 (1994). Parallel provisions exist in the other WTO agreements. The process is mediated and expanded upon by the WTO Dispute Resolution Body through the Dispute Settlement Understanding. Understanding on Rules and Procedures Governing the Settlement of Disputes, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 2, 1869 U.N.T.S. 401 [hereinafter DSU].

105. DSU, *supra* note 104, art. 22.4 (suspension of concessions to be "equivalent to the level of nullification or impairment"). There are, however, exceptions, such as Article 4.1 of the Agreement on Subsidies and Countervailing Measures. Agreement on Subsidies and Countervailing Measures, art. 4.1, Apr. 15, 1994, Marrakesh Agreement Establishing the World Trade Organization, Annex 1A, 1869 U.N.T.S. 14. *See also* Decision by the Arbitrator, *United States–Subsidies on Upland Cotton,* ¶ 4.107, WTO Doc. WT/DS267/ARB/2 (adopted Aug. 31, 2009).

106. Howell E. Jackson, *Substituted Compliance: The Emergence, Challenges, and Evolution of a New Regulatory Paradigm*, 1 J. FIN. REG. 169 (2015); MICHAEL BARR ET AL., FINANCIAL REGULATION: LAW AND POLICY 458 (Robert C. Clark et al. eds., 2016).

in the United States to hold minimum capital reserves,[107] the European Commission proposed an equivalent amendment to its own banking rules in late 2016.[108] This response represents a reciprocal suspension of a benefit granted to U.S. banks, similar in nature to retaliation within the WTO.

5. Penalization

Finally, penalization refers to the case where the defector is punished and where the denial or withdrawal of benefits is not conditioned upon compliance, but where a deterrent effect is the main objective. As already mentioned, economic sanctions can be conditional, but they may also be punitive, as against Russia after its annexation of Crimea.[109] In addition to suspending trade or access to financial markets, under penalization, a nation may seek to impose a disadvantage directly on a defector. In domestic legal systems, this is the purview of the criminal law, typically made effective through fines, imprisonment, or community service. In international law, the equivalent is the use of force. A recent example was the debate in 2016 in the United States, United Kingdom, and France about whether to bomb Syrian forces loyal to President Bashar al-Assad after it was confirmed that chemical weapons had been used against enemy combatants and civilians.[110] In the end, no action was taken. In contrast to suspension or curtailment of benefits, the use of force is prohibitively expensive and can have far-reaching consequences. Penalization through economic sanctions likewise imposes high costs. Fortunately, the above analysis shows how other forces are at work and demonstrates that there are a multitude of ways, besides force and sanction, through which membership value can be suspended when a defector is identified.

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107. Adopted pursuant to section 165 of the Dodd-Frank Wall Street Reform and Consumer Protection Act 2010, Pub. L. No. 111-203, 124 Stat. 1376 (2010).

108. Barker et. al., *EU to Retaliate Against US Bank Capital Rules*, FT (Nov. 21, 2016), https://www.ft.com/content/26078750-b003-11e6-a37c-f4a01f1b0fa1. The proposals concern changes to the Capital Requirements Regulation (575/2013), the Capital Requirements Directive (2013/36/EU), the Bank Recovery and Resolution Directive (2014/59/EU), and the Single Resolution Mechanism Regulation (809/2014).

109. EU Foreign Affairs Council, *Council condemns the illegal referendum in Crimea* (Mar. 17, 2017), http://www.consilium.europa.eu/en/meetings/fac/2014/03/17/. Russia could retreat from Crimea, which would lift sanctions and hence give them a conditional nature, but it is unlikely they were instituted with an expectation that this would occur.

110. Michael Gordon et al., *Dozens of U.S. Missiles Hit Air Base in Syria*, N.Y. TIMES (Apr. 6, 2017), https://www.nytimes.com/2017/04/06/world/middleeast/us-said-to-weigh-military-responses-to-syrian-chemical-attack.html?mcubz=0.

C. *Excluded Benefits*

This section will look at what types of benefits may be suspended under the aforementioned types of enforcement action. First, primary benefits are of course the main type of benefits from which a deviating party will be excluded. Because the focus of this Note is on IEL, the above discussion has mainly considered financial and economic sanctions, including trade and denial of market access. Other sanctions, corresponding to primary benefits in other fields, could range from suspending joint river management among neighbors to refusing to receive citizens denied asylum in other countries. Yet the difficulty with many such regimes is that their benefits are not equally sought or equally distributed. This makes strict reciprocity impossible. Trade—and IEL more broadly—is an exception. All countries have goods to trade, access to markets to offer as incentives, and are concerned with their economic growth. As has been emphasized so far, because the international system operates on the basis of granting or denying access to membership benefits, it should be no surprise that some of the most effective international institutions are those operating within IEL.[111]

Turning to a consideration of ancillary benefits, only participation gains are of great relevance in the context of exclusion. The reason is that this Note uses a typology of enforcement that differs from most others found in the literature.[112] For example, this Note does not consider reputational loss to be the consequence of an enforcement action because reputational loss is not imposed, but follows automatically from the breach itself.[113] The same is true for global standing and coordination gains. The deviating party, by definition, is no longer coordinating. However, following Brummer, this Note does take account of organizational "membership sanctions"[114] as a means to curtail participation gains. In structured regimes, this can be a powerful tool. As noted, the IMF Articles allow for the suspension of voting

111. Although, as the stalled 2001 Doha Development Round illustrates, beyond the basics, a great divergence of interests remains between the Global North and Global South. *See, e.g.*, Robert Hunter Wade, *What Strategies Are Viable for Developing Countries Today? The World Trade Organization and the Shrinking of 'Development Space,'* 10 REV. INT'L POL. ECON. 621, 624 (2003).

112. BRUMMER, SOFT LAW, *supra* note 21, at 145-61; ALEXANDER ET AL., *supra* note 20, at 143-45; GUZMAN, HOW INTERNATIONAL LAW WORKS, *supra* note 8, at 33-55.

113. *Cf.* BRUMMER, SOFT LAW, *supra* note 21, at 145-48. Guzman however recognizes this point, GUZMAN, HOW INTERNATIONAL LAW WORKS, *supra* note 8, at 33. Rather, the sanction is the subsequent risk-weighting, *supra* Section III:B(3).

114. BRUMMER, SOFT LAW, *supra* note 21, at 158-61.

rights, as well as compulsory withdrawal.[115] But, as Brummer points out, the only member ever to be expelled by the IMF and the World Bank was Czechoslovakia, in 1954, although Zimbabwe had its voting rights suspended between 2003 and 2009 because of unpaid arrears.[116]

Whether this lack of use implies that membership sanctions are mostly useless or that they function as a powerful deterrent is difficult to establish. Some evidence can be gleaned from the Financial Action Task Force (FATF). In 2000, the FATF threatened Austria with expulsion from its parent organization, the Organization for Economic Cooperation and Development (OECD), for non-compliance with money-laundering directives.[117] Austria conformed with the FATF's demands within the same year, and its parliament passed legislation to bring Austria into full compliance by 2005.[118] It can certainly be expected that expulsion from a high-profile organization could have a significant impact on the global standing of a country.[119] Even more importantly, in the case of a democracy, the government of the day may suffer considerable domestic political backlash.

Unfortunately, most international organizations strive to be inclusive, representative, and universal in order to gain greater clout and legitimacy. This runs counter to their ability to leverage exclusion of membership as a potent threat. Together with the facts that expulsion or the threat thereof may not encourage a potential defector towards further cooperation and often requires sufficient consensus from other members,[120] the success of the FATF would appear hard to replicate for many other organizations. For these reasons, the relative lack of membership sanctions among today's international bodies is, therefore, unlikely to be a sign of the remedy's impotency as a deterrent. To the contrary, and as is further argued below, international organizations should not hesitate to employ membership sanctions more frequently in order to strengthen their capacity to induce compliance.

But leveraging participation gains in order to achieve positive rather than negative conditionality may be more effective. The International Organization of Securities Commissions (IOSCO) has adopted screening procedures when members sign up to join, requiring the member

115. Articles of Agreement of the IMF, *supra* note 78, art. 26, § 2(c).

116. BRUMMER, SOFT LAW, *supra* note 21, at 160.

117. ALEXANDER ET AL., *supra* note 20, at 70.

118. *Id.*

119. Consistent with the typology above, this would amount to a punitive sanction, where loss of membership in an international organization would have an outsize impact on global standing.

120. BRUMMER, SOFT LAW, *supra* note 21, at 160-61.

to certify that the member is legally empowered in its home jurisdiction to comply with the membership requirements.[121] These requirements are set out in the Multilateralized Memorandum of Understanding, which the members are required to sign.[122] Answers are reviewed, and members are categorized either in "Appendix A" or "Appendix B" depending on whether they comply or not, which creates an incentive to conform. The EU is another good example of how the overall membership benefits of the single market continue to incentivize vital governance and anti-corruption reforms among many Eastern European countries. Requiring robust entrance standards (reliance on positive conditionality) can therefore be as effective as the threat of expulsion (relying on negative conditionality).

In conclusion, therefore, in addition to primary benefits, participation gains are those that can be most readily excluded when enforcement action is taken.

D. *Publicity and Monitoring*

Having sought to present an overview of the legal tools of enforcement available within the international system, as well as what types of benefits these may exclude from a deviant agent, it is important to also note that enforcement ultimately depends to a large extent on good monitoring and sufficient data-gathering.[123] A number of formal mechanisms, such as the IMF/World Bank FSAP surveillance,[124] and a number of informal mechanisms, such as the reporting by non-governmental organizations (NGOs), the press, and academics, contribute to the monitoring process.[125] These entities are important also from the perspective of publicity because monitoring cannot operate if it is not made visible. Publicity processes thus contribute to compliance insofar as they broadcast and make defections known. Because theoretical presumptions of full information must be relaxed in the real world, what is usually referred to as "naming and shaming" can be an effective way to draw attention to defectors in an increasingly crowded informational sphere and to ensure that reputational losses are fully felt by those defectors.

121. BRUMMER, SOFT LAW, *supra* note 21, at 174.

122. *Id.*

123. *Id.* at 161-62.

124. For a detailed consideration and critique see *id.* at 162-71.

125. *Id.* at 175-77; CHAYES & CHAYES, *supra* note 39, at 250-70.

Peer review is both a monitoring and a publicity process that has become increasingly popular. For many organizations, such as the Financial Stability Board (FSB) and the FATF, peer review provides a simple yet effective way of monitoring where regularized reviews create incentives for progress and internal competition, as well as an opportunity for regulators to learn from each other.[126]

E. *Further Considerations*

Given the breadth of literature on legal architecture and compliance, it is not possible nor of interest in the limited space available here to give adequate consideration to all aspects which contribute to enhancing compliance. Yet, before moving on to reflect on the implications of the above discussions, for the sake of comprehensiveness and in acknowledgment of the multiplicity of factors involved, three brief points will be made.

First, if, as assumed, nations comply with international law out of a sense of obligation, then increased legitimacy of rules and norms will inevitably increase compliance.[127] Insofar as such increased legitimacy relates to representation, it will also foster buy-in by more actors, which is an area of concern in a system where rules are often created by wealthier nations who may impose costly rules on poorer ones.[128] Transparency essentially has the same effect as legitimacy, or is a direct contributor to it, and constitutes a central pillar of the Chayeses' managerial approach.[129]

Second, recalling the previous discussion of the work of Abbott et al., more precise wording limits the discretion of the norm-subject to reinterpret its obligation at a later date, increasing the enforceability of the original agreement.[130] Third, the authors also rightly emphasize the delegation of adjudicative or interpretive authority to third parties as an important consideration when aiming to foster increased compliance.[131]

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126. BRUMMER, SOFT LAW, *supra* note 21, at 171-75.

127. FRANCK, *supra* note 7.

128. ALEXANDER ET AL., *supra* note 20, at 152-54.

129. CHAYES & CHAYES, *supra* note 39, at 135-53.

130. Abbott et al., *supra* note 20, at 412*; see also* Abbott & Snidal, *supra* note 94, at 442 (arguing that imprecision is employed by the negotiating parties in order to respond to future uncertainty); ALEXANDER ET AL., *supra* note 20, at 139.

131. Abbott & Snidal, *supra* note 94, at 433-34; ALEXANDER ET AL., *supra* note 20, at 140-41.

F. *Implications*

This section will move on from considering what non-violent enforcement means and how it can be achieved to teasing out some of the implications of the above discussion by briefly examining two case studies of the FATF and the WTO. The section will then look at the international organizational landscape as a whole to argue that there is a high degree of correlation between, on the one hand, strong enforcement or exclusion powers, and, on the other hand, strong membership value. Before concluding, the Note will then offer some thoughts on how these examples can help us understand how to effectively structure future legal regimes, as well as reform current ones, in order to achieve maximum compliance.

The FATF has been hailed as one of the most successful international rule-making bodies thanks to its impressive record of compliance. The above analysis helps explain why. The FATF was set up by the G7 nations in 1989 to fight international financial crime, notably money-laundering and, after the September 11 attacks in 2001, has focused increasingly on terrorist financing as well.[132] As noted, its Secretariat is housed by the OECD,[133] and all OECD countries are members, plus the European Commission and the Gulf Cooperation Council.[134] Its *Recommendations*,[135] first promulgated in 1990, "have been adopted by more than 130 countries and serve as the international anti-money laundering standard."[136] The reason for this success is a combination of powerful enforcement structures.

First, the FATF boasts "[t]he most robust and famous form of formal peer review . . . ." among like international regulatory bodies.[137] Members must adhere to the *Recommendations* and undertake evaluations monitoring their implementation, including on-site visits by FATF staff over a two-week period.[138] Second, as already pointed out, it has access

132. ALEXANDER ET AL., *supra* note 20, at 67, 69, 73.

133. Fin. Action Task Force, *FATF Secretariat,* http://www.fatf-gafi.org/about/fatfsecretariat/ (last visited Sept. 30, 2017).

134. Fin. Action Task Force, *Members and Observers,* http://www.fatf-gafi.org/about/membersandobservers/ (last visited Sept. 30, 2017).

135. The latest version was adopted in 2012 and had been updated several times since. *See* Fin. Action Task Force, *International Standards on Combating Money Laundering and the Financing of Terrorism & Proliferation*: *The FATF Recommendations* (June 2017), http://www.fatfgafi.org/publications/fatfrecommendations/documents/fatf-recommendations.html.

136. ALEXANDER ET AL., *supra* note 20, at 68.

137. BRUMMER, SOFT LAW, *supra* note 21, at 173.

138. *Id.* at 173-74.

to full membership sanctions through its ability to expel non-compliers. Third, it has effectively been able to "name and shame" several jurisdictions. The approach proved effective in the case of Turkey in 1996, where, after five years of fruitless negotiations, a press release advising financial institutions to scrutinize Turkish transactions jolted the government into quick action to comply with its recommendations.[139] The previously discussed threat to expel Austria is likewise telling, and, in 2000, the FATF drew up a "blacklist" of fifteen non-cooperative countries and territories (NCCTs), which has since been reviewed and updated several times.[140] However, the blacklist not only relies on naming and shaming, but also on the FATF's power to condition, restrict, or outright prohibit financial transactions with NCCTs among its members.[141]

It can be surmised that the FATF's power of negative conditionality has had a considerable impact. Based on the above examples, its strong membership sanctions and name-and-shame provisions may also have played an important role. But the overall conclusion that can be drawn from the FATF's success in these areas merely confirms the obvious: where governments are willing to invest resources in a regulatory body to give it proper powers of sanction, it is able to obtain results. Furthermore, targeted FATF jurisdictions tend to be small or developing, and only against a few were sanctions ultimately implemented.[142] The price for following through and withdrawing market access vis-à-vis these jurisdictions was, thus, low.

Another body widely praised for its effectiveness is the WTO. As has already been discussed, it enjoys two distinct advantages: its primary benefits, trade in goods and reduced tariffs, are both widely dispersed and widely sought after. This means most countries will be able to gain substantive primary benefits from joining, and they will also be able to suspend benefits towards other members, allowing for reciprocity. In addition, to accede to the WTO, a country must join "the single undertaking," comprised of the GATT, the General Agreement on Services (GATS), the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS), and several related treaties and understandings that clarify how these agreements operate.[143] Countries

139. ALEXANDER ET AL., *supra* note 20, at 70.

140. BRUMMER, SOFT LAW, *supra* note 21, at 155-57.

141. *Id.* at 157.

142. *Id.* at 156-57.

143. Appellate Body Report, *Brazil–Measures Affecting Desiccated Coconut*, 11-13, WTO Doc. WT/DS22/AB/R (adopted Mar. 20, 1997).

therefore cannot pick and choose among the rules that suit them best, and this means that WTO membership exerts the same type—if not the same magnitude—of conditionality as EU membership or eligibility under the GSP regime. Moreover, this is the same effect observed in modern regional trade agreements, where trade and market access are used as a "magnet" by which to draw in and anchor other commitments on competition law, intellectual property rights, or labor rights.[144]

To what extent can these characteristics and conditions be replicated elsewhere in the international system, in order to encourage effective compliance? Returning to the question of public goods, the same dynamic operates as in relation to reputational gains. Because, per definition, the benefits of public goods are shared widely, there is no possibility of exclusion and, therefore, no opportunity for conditionality. Agreements like the Kyoto Protocol or the Paris Agreement, promulgated in order to curb climate change, therefore impose negative membership value on the individual country because the individual country will enjoy the benefits of the agreements regardless of its own participation.[145] To the extent that we therefore do see compliance with public goods agreements on climate change, the oceans, global systemic risk,[146] or nuclear non-proliferation, such compliance must be motivated by either one, or both, of the following two phenomena. First, international actors might comply out of obligation. Second, they may, contrary to short-term, rationalist presumptions, be able to discern what this Note has referred to as system value,[147] meaning they are able to value the indirect and long-term benefit to their *own interests* from the existence of a system seeking to minimize global or regional negative effects. This becomes evident when studying the chart presented in Figure 1. The chart compares the ability of the relevant organization to enforce norms with the membership value of the

144. R. Michael Gadbaw, *Systemic Regulation of Global Trade and Finance: A Tale of Two Systems*, 13 J. INT'L ECON. L. 551, 567, 571 (2010); *see also* Jeffrey J. Schott, *TPP and the Environment*, Cathleen Cimino-Isaacs, *Labor Standards in the TPP*, and R. Michael Gadbaw, *Competition Policy*, *in* 2 ASSESSING THE TRANS-PACIFIC PARTNERSHIP: INNOVATIONS IN TRADING RULES 33; 41; 82 (Jeffrey J. Schott & Cathleen Cimino-Isaacs eds., 2016), https://piie.com/system/files/documents/piieb16-4.pdf.

145. The only exception would occur where a major polluter, such as the United States, India, or China decides not to take part. Their relative importance may impact the agreement to an extent where the gains from the agreement are substantially impaired where the country's participation is absent.

146. ALEXANDER ET AL., *supra* note 20, at 176 (noting that "[s]ystemic risk is to financial markets what dirty smoke is to the environment . . . ." and thereby presents an externality).

147. *See supra* Section II:E.

underlying regime. It illustrates how strong enforcement correlates with strong membership value, and vice versa.

FIGURE 1:
INTERNATIONAL ORGANIZATIONS

	Strong enforcement	**Weak enforcement**
Strong membership value	A WTO EU FATF Apple App Store IMF/World Bank Finance	B OPEC Basel Committee
Weak membership value	C	D IOSCO United Nations ILO IMF/World Bank G8 (G7)

Note that the chart tracks only organizational entities. Unstructured, market-based legal regimes[148] would be spread across (B) and (D) because they lack a legal framework. They are subject to risk-weighting, but not to the stronger disciplines of enforcement such as conditionality, reciprocity, or penalization.

The inclusion in (B) of the Organization of the Petroleum Exporting Countries (OPEC) reflects the fact that cartels are extremely valuable for their members but are driven purely by the membership gains obtained from the regime in question. Similarly, the inclusion of the Basel Committee in (B) and the Basel III Capital Requirements the Committee seeks to enforce among its member regulators, reflects the fact that these members see increased capital standards as beneficial not only for global financial stability, but also for domestic financial stability as well. Furthermore, many are keen to bring their own regulations in line with global standards. The Basel III regime, therefore, provides both primary and coordinative benefits to its adopters, and probably reputational benefits and global standing as well. Yet the Basel Committee would struggle to discipline a wayward member beyond the employment of limited membership sanctions and the inherent incentives of coordination, reputation, and global standing.

148. Discussed in Section II:C *supra.*

This is the reason the Committee finds itself in (B) and not (A). Furthermore, had market-based regimes been included, a standard for international private banks of capital requirements exceeding those set out in Basel III would have appeared because, even historically, median bank capitalization has exceeded the Basel III requirements.[149]

The paucity of organizations in (C) is as illustrative of the link between enforcement and membership value as the array of institutions aligned in (A). The characteristics of these organizations have all been discussed but for the Apple App Store. Its inclusion as an international organization is no doubt questionable, but it demonstrates that the analysis applies in equal measure to private and commercial operators. Analogous to the case of the EU, the App Store illustrates how market access can be leveraged by private firms with market dominance to impose conditionality and consequently enforce fee, content, and coding requirements.[150] It also provides a reminder that much of global regulation and standard-setting are done by private companies, operating under the same types of incentives as states and regulators.

Finally, (D) represents organizations that have been unable to enforce their rules and principles forcefully due to an inability to either offer or withdraw benefits of substantial import. The G8 or G7 is an example where enforcement action to suspend Russia was taken after the country allegedly violated international law by annexing Crimea. But, as Russia is well aware, the participation value of the G8 is not of a high magnitude, and certainly not sufficient to force it to abandon Crimea or act against what it considers its national interests in eastern Ukraine more generally.

A study of the above chart, even when mindful of the bias flowing from the fact that this Note focuses specifically on IEL, suggests that organizations operating within the ambit of IEL, given their prevalence in (A), possess certain *sui generis* characteristics. As has already been argued, it is suggested that primary gains within IEL, such as increased trade in goods or economic gains more generally, are both widely sought among almost all international actors, and widely attained by them. This allows for conditionality—*i.e.*, the withholding of benefits

149. BRUMMER, SOFT LAW, *supra* note 21, at 150.

150. For an overview of App Store requirements, see APPLE, *App Store Review Guidelines*, https://developer.apple.com/app-store/review/guidelines/ (last visited Sept. 30, 2017). On Apple market share, as well as that of its rival Google Play, see, for example, Lexi Sydow, *Global App Downloads & Consumer Spend Soar in Q1 2017*, APP ANNIE (Apr. 26, 2017), https://www.appannie.com/en/insights/market-data/global-app-downloads-consumer-spend-soar-q1-2017/.

conditioned upon acceptance of certain standards, criteria, or rules. Currently, this is achieved either through the WTO's unique process of reciprocity; through the pooling of resources as in the case of the EU, IMF/World Bank, and FATF; or, lastly, in the context of private consumers and producers, through the acquisition of market share.

However, there remains great scope to enhance these processes. As capital market infrastructure is improving at a rapid pace across the world, such improvement represents a new frontier where the limited but successful usage of capital market sanctions under the FATF demonstrates untapped opportunities. The recent United States-EU banking row also indicates that there are possibilities for reciprocity across a wider spectrum of cooperation than the goods and services trade contained within the WTO. If countries decide to come together around such a framework, they should consider strictly conditioning financial market access on implementation of relevant and related prudential and regulatory standards. Theoretically, it would be possible to also enforce unrelated regulatory standards, such as environmental standards—even though this may be hard to achieve in practice. Nevertheless, as already remarked, some conditioning of market access on, for example, IP, competition, human rights, environmental, and labor standards is currently being pursued within the WTO framework or via free trade deals.[151] It makes sense for countries to seek to leverage the immense value that trade benefits hold for these purposes. Yet, in looking at the FATF, its success partly came from its narrow focus, which allowed the organization to take control of and define the global agenda on financial crime. A specialized World Financial Organization (WFO) may therefore be desirable in order to leverage and coordinate financial market access.[152]

In addition to market access, it is suggested that participation benefits should be used to compel compliance. Expulsion can incur significant losses in global standing for the sanctioned member. International organizations in general arguably make too little use of their ability to sanction defectors by suspending their participation and membership benefits. In addition to negative conditionality, participation benefits should also be leveraged via positive conditionality by

151. *See supra* notes 101 and 144.

152. For further context and arguments why a WFO is desirable, see ALEXANDER ET AL., *supra* note 20, at 155-73; Rosa M. Lastra, *Do We Need a World Financial Organization?*, 17 J. INT'L ECON. L. 787 (2014).

requiring compliance with rules and standards prior to members joining, accompanied by proper review, such as regular peer review. Almost all organizations can lay claim to some amount of meaningful participation gains, and their value as a benefit which can be withdrawn to induce compliance should be better recognized.

Finally, in relation to a WFO, such an organization would provide an opportunity to combine the FSB's peer review with the FSAP standards for monitoring financial regulation. This would ensure both wider compliance with those standards and a boost to their legitimacy, if adopted by a globally representative body.

IV. Conclusion

This Note presents a unified theory of the benefits international actors receive when acceding or adhering to global rules and regulations. By developing the concept of membership value, it suggests that international actors comply with international norms not only because of the substantive gains from the primary objectives those rules and norms seek to address, but also because of the ancillary gains accruing from coordination, reputation, participation, and global standing. Through the concept of system value, the Note also explains why a self-interested global or regional hegemon may seek to sustain a multilateral regime at great direct cost to itself: because it reaps the indirect benefits flowing from stability and predictability. Furthermore, by considering the broader notion of legal regimes in addition to both hard and soft law, the Note showcases the incentives underlying the genesis of not only international laws, but all types of rules, standards, and criteria at the global level. It thereby adds to the literature on why international actors continue to create and adhere to such rules.

In the absence of an international court structure and enforcement by force, the Note also shows how the incentive structures derived from the membership value of legal regimes can be leveraged to achieve compliance through a range of exclusion powers, namely: conditionality, risk-weighting, reciprocity, and penalization. This Note thus demonstrates how legal design and architecture, by relying on such exclusion powers, can enhance compliance beyond the point where marginal benefit would normally equal marginal compliance cost. Based on the foregoing analysis, the Note finds that enforcement is closely linked to the membership value of the underlying regime.

In conclusion, the Note offers some modest suggestions of how these findings should inform our design of future legal regimes and draws particular attention to how the benefits sought by international actors

within international economic regimes are widely dispersed, allowing for effective reciprocity and conditionality. As with goods and services markets in the WTO, this could be leveraged in relation to financial markets. Lastly, the Note argues that participation gains remain an underappreciated benefit, present within most organizational regimes, which, if leveraged through means of conditionality, could enhance compliance with a regime's rules, norms, and regulations.